Notes to the Financial Statements

For the year ended 31 December 2019

1 Corporate information

1.1 General

SANASA Development Bank PLC ("the Bank") is a Licensed Specialised Bank established under the Banking Act No. 30 of 1988. It is a limited liability company, incorporated and domiciled in Sri Lanka. The registered office of the Bank is located at No. 12, Edmonton Road, Colombo 6. The Bank has a primary listing on the Colombo Stock Exchange.

1.2 Principal activities

SANASA Development Bank PLC provides a comprehensive range of financial services encompassing Development Banking, Corporate Banking, Personal Banking, Corporate and Trade Finance, Leasing and other Associated Activities.

1.3 Parent entity and ultimate parent entity

The Bank does not have an identifiable parent of its own.

1.4 Date of authorisation of issue

The Financial Statements for the year ended 31 December 2019 were authorised for issue in accordance with a resolution of the Directors on 26 February 2020.

2 Accounting policies

2.1 Basis of preparation

The Financial Statements have been prepared on a historical cost basis, except for financial assets recognised through other comprehensive income and other financial assets and liabilities held for trading. The Financial Statements are presented in Sri Lankan Rupees (LKR) and all values are rounded to the nearest rupee, except when otherwise indicated.

2.1.1 Changes in accounting policies and disclosures

In these Financial Statements, the Bank has applied SLFRS 16 and IFRIC 23, effective for annual periods beginning on or after 1 January 2019, for the first time.

SLFRS 16 – Leases

SLFRS 16 supersedes LKAS 17 Leases. The standard sets out the principles for the recognition, measurement, presentation and disclosure of leases and requires lessees to recognise most leases on the Statement of Financial Position.

Lessor accounting under SLFRS 16 is substantially unchanged from LKAS 17. Lessors will continue to classify leases as either operating or finance leases using similar principles as in LKAS 17. Therefore, SLFRS 16 did not have an impact for leases where the Bank is the lessor.

The Bank adopted SLFRS 16 using the modified retrospective method of adoption with the date of initial application of 1 January 2019. Under this method, the standard is applied retrospectively with the cumulative effect of initially applying the standard recognised at the date of initial application. The Bank elected to use the transition practical expedient to not reassess whether a contract is or contains a lease at 1 January 2019. Instead, the Bank applied the standard only to contracts that were previously identified as leases applying LKAS 17 and IFRIC 4 at the date of initial application.

The Bank has lease contracts for various branches. Before the adoption of SLFRS 16, the Bank classified each of its leases (as lessee) at the inception date as either a finance lease or an operating lease. Refer to Note 2.3.5 for the accounting policy prior to 1 January 2019.

Upon adoption of SLFRS 16, the Bank applied a single recognition and measurement approach for all leases except for short-term leases and leases of low-value assets. Refer to Note 2.3.5 for the accounting policy beginning 1 January 2019. The standard provides specific transition requirements and practical expedients, which have been applied by the Bank.

Leases previously accounted as operating leases

The Bank recognised right of use assets and lease liabilities for those leases previously classified as operating leases, except for short-term leases and leases of low-value assets. The right of use assets for most leases were recognised based on the carrying amount as if the standard had always been applied, apart from the use of incremental borrowing rate at the date of initial application. In some leases, the right of use assets was recognised based on the amount equal to the lease liabilities, adjusted for any related prepaid and accrued lease payments, discounted using the incremental borrowing rate at the date of initial application.

The Bank also applied the available practical expedients wherein it:

- Used a single discount rate to a portfolio of leases with reasonably similar characteristics
- Relied on its assessment of whether leases are onerous immediately before the date of initial application
- Applied the short-term leases exemptions to leases with lease term that ends within 12 months of the date of initial application
- Excluded the initial direct costs from the measurement of the right of use asset at the date of initial application
- Used hindsight in determining the lease term where the contract contained options to extend or terminate the lease

Based on the above, as at 1 January 2019:

- Right of use assets of LKR 651 Mn. were recognised and presented in the Statement of Financial Position within "Right of use assets".
- Additional lease liabilities of LKR 592 Mn. (included in "Other liabilities") were recognised.
- The adoption of SLFRS 16 had no impact on the Bank's retained earnings and no material impact on its capital adequacy ratio.

IFRIC 23 – Uncertainty over income tax treatment

The interpretation addresses the accounting for income taxes when tax treatments involve uncertainty that affects the application of LKAS 12 "Income Taxes". It does not apply to taxes or levies outside the scope of LKAS 12, nor does it specifically include requirements relating to interest and penalties associated within certain tax treatments. The interpretation specifically addresses the following:

- Whether an entity considers uncertain tax treatments separately
- The assumptions an entity makes about the examination of tax treatments by taxation authorities
- How an entity determines taxable profit (tax loss), tax bases, unused tax losses, unused tax credits and tax rates
- How an entity considers changes in facts and circumstances

The Bank determines whether to consider each uncertain tax treatment separately or together with one or more other uncertain tax treatments and uses the approach that better predicts the resolution of the uncertainty.

The Bank applies significant judgement in identifying uncertainties over income tax treatments. Since the Bank operates in a complex environment, it assessed Bank the interpretation had an impact on its Financial Statements. Upon adoption of the interpretation, the Bank considered whether it has any uncertain tax positions, particularly those relating to transfer pricing. The tax filings of the Bank in different jurisdictions include deductions related to transfer pricing and the taxation authorities may challenge those tax treatments. The Bank determined, based on its tax compliance and transfer pricing study, that it is probable that its tax treatments will be statements of the accepted by the taxation authorities. The interpretation did not have an impact on the Financial Statements of the Bank.

Except for the changes mentioned above, the Bank has consistently applied the accounting policies for all periods presented in these Financial Statements.

2.1.2 Statement of compliance

The Financial Statements of the Bank which comprise the Statement of Financial Position, Statement of Comprehensive Income, Statement of Changes in Equity, Statement of Cash Flow and significant accounting policies and notes have been prepared in accordance with Sri Lanka Accounting Standards (SLFRSs and LKASs) laid down by The Institute of Chartered Accountants of Sri Lanka and are in compliance with the requirements of the Companies Act No. 07 of 2007. The presentation of the Financial Statements is also in compliance with the requirements of the Banking Act No. 30 of 1988 and amendments thereto.

2.1.3 Presentation of financial statements

The Bank presents its statement of financial position broadly in order of liquidity. An analysis regarding recovery or settlement within 12 months after the Statement of Financial Position date (current) and more than 12 months after the statement of financial position date (non-current) is presented in Note 41.

Financial assets and financial liabilities are offset and the net amount reported in the Statement of Financial Position only when there is a legally enforceable right to offset the recognised amounts and there is an intention to settle on a net basis, or to realise the assets and settle the liability simultaneously. Income and expense is not offset in the Income Statement unless required or permitted by any accounting standard or interpretation, and as specifically disclosed in the accounting policies of the Bank.

2.2 Significant accounting judgments, estimates and assumptions

In the process of applying the Bank's accounting policies, management has exercised judgment and estimates in determining the amounts recognised in the Financial Statements. The most significant uses of judgment and estimates are as follows:

2.2.1 Going concern

The Bank's Management has made an assessment of the Bank's ability to continue as a going concern and is satisfied that the Bank has the resources to continue in business for the foreseeable future. Furthermore, Management is not aware of any material uncertainties that may cast significant doubt upon the Bank's ability to continue as a going concern. Therefore, the Financial Statements continue to be prepared on the going concern basis.

2.2.2 Fair value of financial instruments

Where the fair values of financial assets and financial liabilities recorded on the Statement of Financial Position cannot be derived from active markets, they are determined using judgement is required to establish fair values. The judgements include considerations of liquidity and model inputs such as volatility for longer dated derivatives and discount rates, prepayment rates and default rate assumptions for asset backed securities. The valuation of financial instruments is described in more detail in Note 39.

2.2.3 Impairment losses on loans and advances

The Bank reviews its individually significant loans and advances at each Statement of Financial Position date to assess whether an impairment loss should be recorded in the Income Statement. In particular, management judgement is required in the estimation of the amount and timing of future cash flows when determining the impairment loss. These estimates are based on assumptions about a number of factors and actual results may differ, resulting in future changes to the allowance.

Loans and advances that have been assessed individually and found to be impaired have been provide for the impairment loss on loans and advances as disclosed in Note 7 and Note 16. All individually not insignificant loans and advances and unimpaired individual significant customers are then assessed collectively, in groups of assets with similar risk characteristics, to determine whether provision should be made due to Expected Credit Loss (ECL – applicable from 1 January 2018 onwards) events for which there is objective evidence but whose effects are not yet evident. The collective assessment takes account of data from the loan portfolio (such as levels of arrears, remaining maturity, customer identification number, etc.), and judgments to the effect of concentrations of risks and economic data (including levels of unemployment, gross domestic production, interest rate and exchange rate fluctuation).

2.2.4 Deferred tax assets

Deferred tax assets are recognised in respect of tax losses to the extent that it is probable that taxable profit will be available against which the losses can be utilised. Judgment is required to determine the amount of deferred tax assets that can be recognised, based upon the likely timing and level of future taxable profits, together with future tax planning strategies.

2.2.5 Taxation

The Bank is subject to income taxes and other taxes including VAT on financial services. Significant judgment was required to determine the total provision for current, deferred and other taxes pending the issue of tax guideline on the treatment of the adoption of SLFRSs in the Financial Statements and the taxable profit for the purpose of imposition of taxes. Uncertainties exist, with respect to the interpretation of the applicability of tax laws, at the time of the preparation of these Financial Statements.

The Bank recognised assets and liabilities for current deferred and other taxes based on estimates of whether additional taxes will be due. Where the final tax outcome of these matters is different from the amounts that were initially recorded, such differences will impact the income.

2.2.6 Defined benefit plan

The cost of the defined benefit plan is determined using an actuarial valuation. The actuarial valuation involves making assumptions about discount rates, salary increment rate, age of retirement, and mortality rates. Due to the long-term nature of these plans, such estimates are subject to significant uncertainty. The assumptions used for valuation is disclosed in more detail in Note 28.1.3.

2.2.7 Useful lifetime of the property and equipment

The Bank reviews the residual values, useful lives and methods of depreciation of assets as at each reporting date. Judgment of the management is exercised in the estimation of these values, rates, methods and hence they are subject to uncertainty.

2.3 Summary of significant accounting policies

2.3.1 Foreign currency transactions and balances

The Financial Statements are presented in Sri Lankan Rupees (LKR).

Transactions in foreign currencies are initially recorded at the functional currency rate of exchange ruling at the date of the transaction.

Monetary assets and liabilities denominated in foreign currencies are retranslated at the functional currency rate of exchange at the statement of financial position date. All differences arising on non-trading activities are taken to "Other operating income" in the Income Statement.

2.3.2 Financial instruments

2.3.2.1 Initial recognition, classification and subsequent measurement

(a) Date of recognition

All financial assets and liabilities are initially recognised on the trade date, i.e., the date that the Bank becomes a party to the contractual provisions of the instrument. This includes "regular way trades": purchases or sales of financial assets that require delivery of assets within the time frame generally established by regulation or convention in the market place.

(b) Initial measurement of financial instruments

The classification of financial instruments at initial recognition depends on the purpose and the Management's intention for which the financial instruments were acquired and their characteristics. All financial instruments are measured initially at their fair value plus transaction costs, except in the case of financial assets and financial liabilities recorded at fair value through profit or loss.

(c) "Day 1" profit or loss

When the transaction price differs from the fair value of other observable current market transactions in the same instrument or based on a valuation technique whose variables include only data from observable markets, the bank immediately recognises the difference between the transaction price and fair value ("Day 1" profit or loss) in "Net operating income". In cases where fair value is determined using data which is not observable, the difference between the transaction price and model value is only recognised in the income statement when the inputs become observable, or when the instrument is derecognised.

(d) Classification and subsequent measurement of financial instruments

(i) Financial assets

The Bank classifies its financial assets into the following measurement categories:

- Financial assets fair value through profit or loss
- Financial assets at amortised cost
- Financial assets measured at fair value through other comprehensive income

The classification depends on the Bank's business model for managing financial assets and the contractual terms of the financial assets' cash flows. The Bank classifies its financial liabilities at amortised cost unless it has designated liabilities at fair value through profit.

a. Financial assets fair value through profit or loss

Financial assets fair value through profit or loss comprise:

- Financial investments – for trading;
- Instruments with contractual terms that do not represent solely payments of principal and profit.

Financial instruments held at fair value through profit or loss are initially recognised at fair value, with transaction costs recognised in the Statement of Profit or Loss as incurred. Subsequently, they are measured at fair value and any gains or losses are recognised in the statement of profit or loss as they arise.

Where a financial asset is measured at fair value, a credit valuation adjustment is included to reflect the credit worthiness of the counterparty, representing the movement in fair value attributable to changes in credit risk.

Financial investments – for trading

A financial investment is classified as financial assets recognised through profit or loss if it is acquired or incurred principally for the purpose of selling or repurchasing in the near term, or forms part of a portfolio of financial instruments that are managed together and for which there is evidence of short-term profit taking, or it is a derivative not in a qualifying hedge relationship.

Government securities and investment in unit trust securities are classified as financial assets recognised through profit or loss and recognised at fair value. Refer Note 15.

Financial instruments designated as measured at fair value through profit or loss

Upon initial recognition, financial instruments may be designated as measured at fair value through profit or loss. A financial asset may only be designated at fair value through profit or loss if doing so eliminates or significantly reduces measurement or recognition inconsistencies (i.e. eliminates an accounting mismatch) that would otherwise arise from measuring financial assets or liabilities on a different basis. The Bank does not designate any financial instruments under this category.

b. Financial assets measured at amortised cost

Placements, loans and receivables to other customers and debt and other instruments are measured at amortised cost where they have:

- Contractual terms that give rise to cash flows on specified dates, that represent solely payments of principal and profits on the principal amount outstanding; and
- Are held within a business model whose objective is achieved by holding to collect contractual cash flows.

These instruments are initially recognised at fair value plus directly attributable transaction costs and subsequently measured at amortised cost. The measurement of credit impairment is based on the three-stage expected credit loss model described below in Note 2.3.2.3 impairment of financial assets.

c. Financial assets measured at fair value through other comprehensive income

Investment in equity instruments that are neither trading financial assets recognised through profit or loss, nor contingent consideration recognised by the Bank in a business combination to which SLFRS 3 "Business Combination" applies, are measured at fair value through other comprehensive income, where an irrevocable election has been made by Management due to long-term nature of investment. For portfolios where Management does not consider an irrevocable election of adopting fair value through other comprehensive income, by default such investments shall be measured at fair value through profit and loss.

Amounts presented in other comprehensive income are not subsequently transferred to profit or loss. Dividends on such investments are recognised in profit or loss.

(ii) Financial liabilities

The initial and subsequent measurement of financial liabilities depends on their classification as described below:

At the inception the Bank determines the classification of its financial liabilities. Accordingly, financial liabilities are classified as;

- Financial liabilities at Fair Value through Profit or Loss (FVTPL)
  - Financial liabilities held for trading
  - Financial liabilities designated at fair value through profit or loss
- Financial liabilities at amortised cost

The subsequent measurement of financial liabilities depends on their classification.

a. Financial liabilities at Fair Value through Profit or Loss (FVTPL)

Financial liabilities at FVTPL include financial liabilities held for trading and financial liabilities designated upon initial recognition at fair value through profit or loss. Subsequent to initial recognition, financial liabilities at FVTPL are fair value, and changes therein recognised in profit or loss.

Financial liabilities are classified as held for trading if they are acquired principally for the purpose of selling or repurchasing in the near term or holds as a part of the portfolio that is managed together for short term profit or position taking. This category includes derivative financial instruments entered in to by the Bank which are not designated as hedging instruments in the hedge relationships as defined by the Sri Lanka Accounting Standards – LKAS 39 on "Financial Instruments: Recognition and Measurements". Separated embedded derivatives are also classified as held for trading unless they are designated as effective hedging instruments. Gains or losses on liabilities held for trading are recognised in the income statement.

The Bank does not have any financial liabilities under this category.

b. Financial liabilities at amortised cost

Financial instruments issued by the Bank that are not designated at fair value through profit or loss, are classified as liabilities at amortised cost under "due to customers and other borrowings" as appropriate, where the substance of the contractual arrangement results in the Bank having an obligation either to deliver cash or another financial asset to the holder, or to satisfy the obligation other than by the exchange of a fixed amount of cash or another financial assets for a fixed number of own equity shares at amortised cost using EIR method.

After initial recognition, such financial liabilities are substantially measured at amortised cost using the EIR method. Amortised cost is calculated by taking into account any discount or premium on the issue and costs that are integral part of the EIR. The EIR amortisation is included in "interest expenses" in the Income Statement. Gains and losses are recognised in the Income Statement when the liabilities are derecognised as well as through the EIR amortisation process.

This category consists of due to other customers, other borrowings, debt securities issued and subordinated term debts.

2.3.2.2 De-recognition of financial instruments

(a) Financial assets

A financial asset (or, where applicable a part of a financial asset or part of a group of similar financial assets) is derecognised when:

- The rights to receive cash flows from the asset have expired.
- The Bank has transferred its rights to receive cash flows from the asset or has assumed an obligation to pay the received cash flows in full without material delay to a third party under a "pass–through" arrangement; and either:
- The Bank has transferred substantially all the risks and rewards of the asset, or
- The Bank has neither transferred nor retained substantially all the risks and rewards of the asset, but has transferred control of the asset.

When the Bank has transferred its rights to receive cash flows from an asset or has entered into a pass–through arrangement and has neither transferred nor retained substantially all the risks and rewards of the asset nor transferred control of the asset, the asset is recognised to the extent of the Bank's continuing involvement in the asset. In that case, the Bank also recognises an associated liability. The transferred asset and the associated liability are measured on a basis that reflects the rights and obligations that the Bank has retained. Continuing involvement that takes the form of a guarantee over the transferred asset is measured at the lower of the original carrying amount of the asset and the maximum amount of consideration that the Bank could be required to repay.

(b) Financial liabilities

A financial liability is derecognised when the obligation under the liability is discharged or cancelled or expires. Where an existing financial liability is replaced by another from the same lender on substantially different terms, or the terms of an existing liability are substantially modified, such an exchange or modification is treated as a derecognition of the original liability and the recognition of a new liability. The difference between the carrying value of the original financial liability and the consideration paid is recognised in profit or loss.

2.3.2.3 Impairment of financial assets

The Bank applies a three-stage approach to measuring Expected Credit Losses (ECLs) for the following categories of financial assets (debt instruments) that are not measured at fair value through profit or loss:

- Instruments measured at amortised cost and fair value through other comprehensive income;
- Loans and receivables to other customers; and
- Financial guarantee contracts

ECL is not recognised on equity instruments.

Financial assets migrate through the following three stages based on the change in credit risk since initial recognition:

Stage 1: 12 months ECL

For exposures where there has not been a significant increase in credit risk since initial recognition and that are not credit impaired upon origination, the portion of the lifetime ECL associated with the probability of default events occurring within the next 12 months is recognised.

Bank determines 12 months ECL from customers who are not significantly credit deteriorated (i.e. less than 30 days past due).

Stage 2: Lifetime ECL – not Credit Impaired

Credit facilities, where contractual payments of a customer are more than 30 days past due, other than the credit facilities categorised under Stage 3 below, subject to the rebuttable presumption as stated in SLFRS 9. All restructured loans, which are restructured up to two times (other than upgraded restructured facilities, satisfactory performing period of a minimum 90 days considered subsequent to the due date of the 1st capital and/or interest instalment post-restructure). Under-performing credit facilities/exposures.

Stage 3: Lifetime ECL – Credit Impaired

Credit facilities where contractual payments of a customer are more than 90 days past due or three instalments in arrears, subject to the rebuttable presumption as stated in SLFRS 9. All restructured loans, which are restructured more than twice. All rescheduled loans, other than credit facilities/exposures (other than upgraded restructured facilities, satisfactory performing period of a minimum 90 days considered subsequent to the due date of the 1st capital and/or interest instalment post-restructure). All credit facilities/customers classified as non-performing as per CBSL Directions. Non-performing credit facilities/customers.

Determining the stage for impairment

At each reporting date, the Bank assesses whether there has been a significant increase in credit risk for exposures since initial recognition by comparing the risk of default occurring over the expected life between the reporting date and the date of initial recognition. The Bank considers reasonable and supportable information that is relevant and available without undue cost or effort for this purpose. This includes quantitative and qualitative information and also, forward-looking analysis.

An exposure will migrate through the ECL stages as asset quality deteriorates. If, in a subsequent period, asset quality improves and also reverses any previously assessed significant increase in credit risk since origination, then the provision for impairment loss reverts from lifetime ECL to 12 months ECL. Exposures that have not deteriorated significantly since origination, or where the deterioration remains within the Bank's investment grade criteria, or which are less than 30 days past due, are considered to have a low credit risk. The provision for impairment loss for these financial assets is based on a 12 months ECL.

When an asset is uncollectible, it is written off against the related provision. Such assets are written off after all the necessary procedures have been completed and the amount of the loss has been determined. Subsequent recoveries of amounts previously written off reduce the amount of the expense in the statement of profit or loss.

The Bank assesses whether the credit risk on an exposure has increased significantly on an individual or collective basis. For the purposes of a collective evaluation of impairment, financial instruments are grouped on the basis of shared credit risk characteristics, taking into account instrument type, credit risk ratings, date of initial recognition, remaining term to maturity, industry, geographical location of the borrower and other relevant factors.

Measurement of ECLs

ECLs are derived from unbiased and probability-weighted estimates of expected loss, and are measured as follows:

- Financial assets that are not credit-impaired at the reporting date: as the present value of all cash shortfalls over the expected life of the financial asset discounted by the effective rate. The cash shortfall is the difference between the cash flows due to the Bank in accordance with the contract and the cash flows that the Bank expects to receive.
- Financial assets that are credit-impaired at the reporting date: as the difference between the gross carrying amount and the present value of estimated future cash flows discounted by the effective rate.
- Undrawn commitments: as the present value of the difference between the contractual cash flows that are due to the Bank if the commitment is drawn down and the cash flows that the Bank expects to receive.
- Financial guarantee contracts: as the expected payments to reimburse the holder less any amounts that the Bank expects to recover.

For further details on how the Bank calculates ECLs including the use of forward looking information, refer to the impairment assessment section in Note 42.

ECLs are recognised using a provision for impairment loss account in Statement of Profit and Loss. The Bank recognises the provision charge in statement of profit or loss, with the corresponding amount recognised in other comprehensive income, with no reduction in the carrying amount of the asset in the Statement of Financial Position.

The mechanics of the ECL calculations are outlined below and the key elements are, as follows:

PD : The probability of Default is an estimate of the likelihood of default over a given time horizon. A default may only happen at a certain time over the assessed period, if the facility has not been previously derecognised and is still in the portfolio.

EAD : The Exposure at Default is an estimate of the exposure at a future default date, taking into account expected changes in the exposure after the reporting date, including repayments of capital and financing income, whether scheduled by contract or otherwise, expected draw downs on committed facilities, and accrued financing income from missed payments.

LGD : The Loss Given Default is an estimate of the loss arising in the case where a default occurs at a given time. It is based on the difference between the contractual cash flows due and those that the Bank would expect to receive, including the realisation of any collateral.

2.3.2.4 Critical accounting assumptions and estimates applicable for financial instruments

The application of the Bank's accounting policies requires the use of judgements, estimates and assumptions. If different assumptions or estimates were applied, the resulting values would change, impacting the net assets and income of the Bank.

Assumptions made at each reporting date are based on best estimates at that date. Although the Bank has internal control systems in place to ensure that estimates are reliably measured, actual amounts may differ from those estimates. Estimates and underlying assumptions are reviewed on an on-going basis. Revisions to accounting estimates are recognised in the period in which the estimates are revised and in any future periods affected.

The accounting policies which are most sensitive to the use of judgement, estimates and assumptions are specified below.

(a) Fair value measurement

A significant portion of financial instruments are carried on the statement of financial position at fair value. Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date.

Where the classification of a financial asset or liability results in it being measured at fair value, wherever possible, the fair value is determined by reference to the quoted bid or offer price in the most advantageous active market to which the Bank has immediate access. An adjustment for credit risk is also incorporated into the fair value as appropriate.

Fair value for a net open position that is a financial liability quoted in an active market is the current offer price, and for a financial asset the bid price, multiplied by the number of units of the instrument held or issued.

Where no active market exists for a particular asset or liability, the Bank uses a valuation technique to arrive at the fair value, including the use of transaction prices obtained in recent arm's length transactions, discounted cash flow analysis, option pricing models and other valuation techniques, based on market conditions and risks existing at reporting date. In doing so, fair value is estimated using a valuation technique that makes maximum use of observable market inputs and places minimal reliance upon entity-specific inputs.

The best evidence of the fair value of a financial instrument at initial recognition is the transaction price (i.e. the fair value of the consideration given or received) unless the fair value of that instrument is evidenced by comparison with other observable current market transactions in the same instrument (i.e. without modification or repackaging) or based on a valuation technique whose variables include only data from observable markets. When such evidence exists, the Bank recognises the difference between the transaction price and the fair value in profit or loss on initial recognition (i.e. on day one).

(b) Impairment charges on loans and receivables to other customers

Judgement is required by management in the estimation of the amount and timing of future cash flows when determining an impairment loss for loans and receivables to other customers. In estimating these cash flows, the Bank makes judgments about the customer's financial situation and the net realisable value of collateral. These estimates are based on assumptions about a number of factors and actual results may differ, resulting in future changes to the impairment allowance.

A collective assessment of impairment takes into account data from the advance portfolio (such as credit quality, levels of arrears, credit utilisation, advances to collateral ratios etc.), and concentrations of risk and economic data (including levels of unemployment, inflation, GDP growth rate, country risk and the performance of different individual groups). The impairment loss on loans and receivables to other customers is disclosed in more detail in Note 16.

2.3.2.5 Determination of fair value

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The fair value measurement is based on the presumption that the transaction to sell the asset or transfer the liability takes place either:

- In the principal market for the asset or liability, or
- In the absence of a principal market, in the most advantageous market for the asset or liability

The principal or the most advantageous market must be accessible by the Bank. The fair value of an asset or a liability is measured using the assumptions that market participants would use when pricing the asset or liability, assuming that market participants act in their economic best interest. A fair value measurement of a non-financial asset takes into account a market participant's ability to generate economic benefits by using the asset in its highest and best use or by selling it to another market participant that would use the asset in its highest and best use.

The Bank uses valuation techniques that are appropriate in the circumstances and for which sufficient data are available to measure fair value, maximising the use of relevant observable inputs and minimising the use of unobservable inputs.

All assets and liabilities for which fair value is measured or disclosed in the Financial Statements are categorised within the fair value hierarchy, described as follows, based on the lowest level input that is significant to the fair value measurement as a whole:

Level 1 – Quoted (unadjusted) market prices in active markets for identical assets or liabilities

Level 2 – Valuation techniques for which the lowest level input that is significant to the fair value measurement is directly or indirectly observable

Level 3 – Valuation techniques for which the lowest level input that is significant to the fair value measurement is unobservable

For assets and liabilities that are recognised in the Financial Statements on a recurring basis, the Bank determines whether transfers have occurred between levels in the hierarchy by reassessing categorisation (based on the lowest level input that is significant to the fair value measurement as a whole) at the end of each reporting period.

The disclosure of fair value of financial instruments is disclosed in Note 39.

2.3.2.6 Collateral valuation

The Bank seeks to use collateral, where possible, to mitigate its risks on financial assets. The collateral comes in various forms such as cash, securities, letters of credit/guarantees, real estate, receivables, inventories, other non-financial assets and credit enhancements such as netting agreements. The fair value of collateral is generally assessed, at a minimum, at inception and based on the guidelines issued by the Central Bank of Sri Lanka. Non-financial collateral, such as real estate, is valued based on data provided by third parties such as independent values and Audited Financial Statements.

Collateral repossessed

The Bank's policy is to determine whether a repossessed asset is best used for its internal operations or should be sold. Assets determined to be useful for the internal operations are transferred to their relevant asset category at the lower of their repossessed value or the carrying value of the original secured asset.

2.3.2.7 Offsetting financial instruments

Financial Assets and Liabilities are offset, and the net amount is presented in the Balance Sheet when the Bank has a legal right to offset the amounts and intends to settle on a net basis or to realise the asset and settle the liability simultaneously. Refer to Note on financial risk management – offsetting of financial assets and liabilities.

2.3.3 Repurchase and reverse repurchase agreements

Securities sold under agreements to repurchase at a specified future date are not derecognised from the Statement of Financial Position as the Bank retains substantially all the risks and rewards of ownership. The corresponding cash received is recognised in the Statement of Financial Position as an asset with a corresponding obligation to return it, including accrued interest as a liability within "repurchase agreements", reflecting the transaction's economic substance as a loan to the Bank. The difference between the sale and repurchase prices is treated as interest expense and is accrued over the life of agreement using the EIR. When the counterparty has the right to sell or replace the securities, the Bank reclassifies those securities in its Statement of Financial Position to "Financial assets held-for-trading pledged as collateral" or to "Financial investments available-for-sale pledged as collateral", as appropriate. Conversely, securities purchased under agreements to resell at a specified future date are not recognised in the Statement of Financial Position. The consideration paid, including accrued interest, is recorded in the Statement of Financial Position, within "reverse repurchase agreements", reflecting the transaction's economic substance as a loan by the Bank.

The difference between the purchase and resale prices is recorded in "Net interest income" and is accrued over the life of the agreement using the EIR. If securities purchased under agreement to resell are subsequently sold to third parties, the obligation to return the securities is recorded as a short sale within "Financial liabilities held-for-trading" and measured at fair value with any gains or losses included in "Net operating income".

2.3.4 Securities lending and borrowing

Securities lending and borrowing transactions are usually collateralised by securities or cash. The transfer of the securities to counterparties is only reflected on the Statement of Financial Position if the risks and rewards of ownership are also transferred. Cash advanced or received as collateral is recorded as an asset or liability. Securities borrowed are not recognised on the Statement of Financial Position, unless they are then sold to third parties, in which case the obligation to return the securities is recorded as a trading liability and measured at fair value with any gains or losses included in "Net operating income".

2.3.5 Leases (Policy applicable before 1 January 2019)

The determination of whether an arrangement is a lease or it contains a lease, is based on the substance of the arrangement and requires an assessment of whether the fulfilment of the arrangement is dependent on the use of a specific asset or assets and the arrangement conveys a right to use the asset.

2.3.5.1 Operating leases

Bank as a lessor

Leases where the Bank does not transfer substantially all the risk and benefits of ownership of the asset are classified as operating leases. Initial direct costs incurred in negotiating operating leases are added to the carrying amount of the leased asset and recognised over the lease term on the same basis as rental income. Contingent rents are recognised as revenue in the period in which they are earned.

2.3.5.2 Finance leases

Bank as a lessor

Assets leased to customers which transfer substantially all the risks and rewards associated with ownership other than legal title, are classified as "Finance Leases". Amounts receivable under finance leases are included under "loans and receivables to customers" in the Statement of Financial Position after deduction of initial rentals received, unearned lease income and the accumulated impairment losses. When assets are held subject to a finance lease, the present value of the lease payments, discounted at the rate of interest implicit in the lease, is recognised as a receivable. The difference between the total payments receivable under the lease and the present value of the receivable is recognised as unearned finance income, which is allocated to accounting periods reflect a constant periodic rate of return.

2.3.6 Cash and cash equivalents

Cash and cash equivalents as referred to in the cash flow statement comprises cash on hand and balances with Banks on demand or with an original maturity of three months or less.

2.3.7 Property, plant and equipment

Property, plant and equipment are tangible items that are held for servicing, or for administrative purposes, and are expected to be used during more than one year.

Property and equipment are recognised if it is probable that future economic benefits associated with the asset will flow to the entity and the cost of the asset can be measured reliably in accordance with LKAS 16 on Property, plant and equipment. Initially property and equipment are measured at cost.

2.3.7.1 Basis of recognition and measurement

Cost model

An item of property, plant and equipment that qualifies for recognition as an asset is initially measured at its costs. Costs include expenditure that is directly attributable to the acquisition of the asset and cost is incurred subsequently to add to or replace a part of it. The cost of self-constructed assets includes the cost of materials and direct labour, any other costs directly attributable to bringing the asset to working condition for its intended use and the costs of dismantling and removing the items and restoring at the site on which they are located and capitalised borrowing costs. Purchase of software that is integral to the functionality of the related equipment is capitalised as a part of computer equipment.

When parts of property, plant and equipment have different useful lives, they are accounted for as separate items (major components) of property, plant and equipment.

The Bank applies the cost model to property, plant and equipment and records at cost of purchase or construction together with any incidental expenses thereon less accumulated depreciation and any accumulated impairment losses.

Changes in the expected useful life are accounted for by changing the amortisation period or method, as appropriate, and treated as changes in accounting estimates.

2.3.7.2 Subsequent cost

These are costs that are recognised in the carrying amount of an item, if it is probable that the future economic benefits embodied within that part will flow to the Bank and it can be reliably measured.

2.3.7.3 Repairs and maintenance

Repairs and maintenance are charged to the profit or loss during the financial period in which they are incurred. The cost of major renovations is included in the carrying amount of the assets when it is probable that future economic benefits in excess of the most recently assessed standard of performance of the existing assets will flow to the Bank and the renovation replaces an identifiable part of the asset. Major renovations are depreciated during the remaining useful life of the related asset.

2.3.7.4 Capital work in progress

Capital work in progress is stated at cost. It would be transferred to the relevant asset when it is available for use, i.e. when it is in the location and condition necessary for it to be capable of operating in the manner intended by Management. Capital work in progress is stated at cost less any accumulated impairment losses.

2.3.7.5 Borrowing costs

As per LKAS 23 on "Borrowing Costs", the Bank capitalises the borrowing costs that are directly attributable to acquisition, construction or production of qualifying assets as part of the cost of the asset. A qualifying asset is an asset which takes a substantial period of time to get ready for its intended use or sale. Other borrowing costs are recognised in the profit or loss in the period in which they occur.

2.3.7.6 De-recognition

Property and equipment is derecognised on disposal or when no future economic benefits are expected from its use. Any gain or loss arising on de-recognition of the asset (calculated as the difference between the net disposal proceeds and the carrying amount of the asset) is recognised in "other operating income" in the income statement in the year the asset is derecognised.

2.3.7.7 Depreciation

Depreciation is calculated using the straight–line method to write down the cost of property and equipment to their residual values over their estimated useful lives. Land is not depreciated. The estimated useful lives are as follows:

Buildings	20 years
Computer hardware	3 years
Machinery and equipment	5 years
Motor vehicles	4 years
Furniture and fittings	5 years

2.3.8 Investment properties

Properties held to earn rental income have been classified as investment properties. Investment properties initially recognised at cost. After initial recognition the Bank uses the cost method to measure all of its investment property in according with requirements in LKAS 16 "Property, plant and equipment".

Investment properties are derecognised when either they have been disposed of or when the investment property is permanently withdrawn from use and no future economic benefit is expected from its disposal. Any gains or losses on the retirement or disposal of an investment property are recognised in the income statement in the year of retirement or disposal.

Transfers are made to investment property when, and only when, there is a change in use, evidenced by the end of owner occupation, commencement of an operating lease to another party or completion of construction or development. Transfers are made from investment property when, and only when, there is a change in use, evidenced by commencement of owner occupation or commencement of development with a view to sale.

Depreciation is calculated using the straight-line method to write down the cost of investment property to their residual values over their estimated useful lives. The estimated useful lives are as follows:

Buildings	20 years

2.3.9 Asset classified as held for sale

Non-current assets are classified as investments - "held for sale" when their carrying amounts will be recovered principally through sale, they are available for sale in their present condition and their sale is highly probable. Non-current assets held for sale are measured at the lower of their carrying amount and fair value less cost to sell, except for those assets and liabilities that are not within the scope of the measurement requirements of SLFRS 5 - "Non-current Assets Held for Sale and Discontinued Operations" such as deferred taxes, financial instruments, investment properties, insurance contracts and assets and liabilities arising from employee benefits.

2.3.10 Intangible assets

The Bank's intangible assets include the value of computer software.

2.3.10.1 Basis of recognition

An intangible asset is recognised only when its cost can be measured reliably and it is probable that the expected future economic benefits that are attributable to it will flow to the Bank in accordance with LKAS 38 on "Intangible Assets".

Intangible assets acquired separately are measured on initial recognition at cost. Following initial recognition, intangible assets are carried at cost less any accumulated amortisation and accumulated impairment losses if any.

2.3.10.2 Subsequent expenditure

Subsequent expenditure on intangible asset is capitalised only when it increases the future economic benefits embodied in the specific asset to which it relates. All other expenditure is expensed as incurred.

2.3.10.3 Useful economic life, amortisation and impairment

The useful lives of intangible assets are assessed to be either finite or indefinite.

Intangible assets with finite lives are amortised over the useful economic life. The amortisation period and the amortisation method for an intangible asset with a finite useful life are reviewed at least at each financial year end. Changes in the expected useful life or the expected pattern of consumption of future economic benefits embodied in the asset are accounted for by changing the amortisation period or method, as appropriate, and they are treated as changes in accounting estimates. The amortisation expense on intangible assets with finite lives is recognised in the income statement in the expense category consistent with the function of the intangible asset.

Amortisation

Amortisation is calculated using the straight-line method to write down the cost of intangible assets to their residual value over their estimated useful life as follows:

The class of intangible assets	Useful life	Amortisation method
Computer software	7 years	Straight-line method

The unamortised balances of intangible assets with finite lives are reviewed for impairment whenever there is an indication for impairment and recognised in profit or loss to the extent that they are no longer probable of being recovered from the expected future benefits.

2.3.10.4 Derecognition

Intangible assets are derecognised on disposal or when no future economic benefits are expected from their use. Any gain or loss arising on derecognition of the asset, (calculated as the difference between the net disposal proceeds and the carrying amount of the asset) is recognised in the profit or loss in the year the asset is derecognised.

2.3.11 Impairment of non-financial assets

The Bank assesses at each reporting date whether there is an indication that an asset may be impaired. If any indication exists, or when annual impairment testing for an asset is required, the Bank estimates the asset's recoverable amount. An asset's recoverable amount is the higher of an asset's or cash-generating unit's (CGU) fair value less costs to sell and its value in use. Where the carrying amount of an asset or CGU exceeds its recoverable amount, the asset is considered impaired and is written down to its recoverable amount. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. In determining fair value less costs to sell, an appropriate valuation model is used.

For assets, an assessment is made at each reporting date as to whether there is any indication that previously recognised impairment losses may no longer exist or may have decreased. If such indication exists, the Bank estimates the asset's or CGU's recoverable amount. A previously recognised impairment loss is reversed only if there has been a change in the assumptions used to determine the asset's recoverable amount since the last impairment loss was recognised. The reversal is limited so that the carrying amount of the asset does not exceed its recoverable amount, nor exceeds the carrying amount that would have been determined, net of depreciation, had no impairment loss been recognised for the asset in prior years. Such reversal is recognised in the income statement.

2.3.12 Financial guarantees

In the ordinary course of business, the Bank gives financial guarantees, consisting of Bank guarantees. Bank guarantees are initially recognised in the financial statements (within "other liabilities") at fair value, being the premium received. Subsequent to initial recognition, the Bank's liability under each guarantee is measured at the higher of the amount initially recognised less, when appropriate, cumulative amortisation recognised in the income statement, and the best estimate of expenditure required settling any financial obligation arising as a result of the guarantee. Any increase in the liability relating to financial guarantees is recorded in the income statement in "Credit loss expense". The premium received is recognised in the income statement in "Net fees and commission income" on a straight line basis over the life of the guarantee.

2.3.13 Provisions

Provisions are recognised when the Bank has a present obligation (legal or constructive) as a result of a past event, and it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate can be made of the amount of the obligation. The expense relating to any provision is presented in the income statement net of any reimbursement.

2.3.14 Retirement benefit obligations

2.3.14.1 Defined benefit plan- gratuity

Based on LKAS 19 on "Employee Benefits", the Bank has adopted the actuarial valuation method for employee benefit liability an actuarial valuation is carried out every year to ascertain the liability. A separate fund is not maintained for this purpose.

The principal assumptions, which have the most significant effects on the valuation, are the rate of discount, rate of increase in salary, rate of turnover at the selected ages, rate of disability, death benefits and expenses.

The liability is measured on an actuarial basis using the projected unit credit method, adjusted for unrecognised actuarial gains and losses. The defined benefit plan liability is discounted using rates equivalent to the market yields at the date of Statement of Financial Position that are denominated in the currency in which benefits will be paid, and that have a maturity approximating to the terms of the related pension liability.

The Bank recognises all actuarial gains and losses arising from the defined benefit plan in other comprehensive income (OCI) and all other expenses related to defined benefit plans are recognised as personnel expenses in income statement.

2.3.14.2 Defined contribution plan – Employees' Provident Fund and Employees' Trust Fund

Employees are eligible for Employees' Provident Fund Contributions and Employees' Trust Fund Contributions in line with the respective Statutes and Regulations. The Bank contributes a minimum 12% and 3%.

2.3.15 Recognition of income and expenses

Revenue is recognised to the extent that it is probable that the economic benefits will flow to the Bank and the revenue can be reliably measured. The following specific recognition criteria must also be met before revenue is recognised.

2.3.15.1 Interest and similar income and expense

For all financial instruments measured at amortised cost, interest bearing financial assets classified as available for sale and financial instruments designated at fair value through profit or loss, interest income or expense is recorded using the EIR, which is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial instrument or a shorter period, where appropriate, to the net carrying amount of the financial asset or financial liability.

The calculation takes into account all contractual terms of the financial instrument (for example, prepayment options) and includes any fees or incremental costs that are directly attributable to the instrument and are an integral part of the EIR, but not future credit losses.

The carrying amount of the financial asset or financial liability is adjusted if the Bank revises its estimates of payments or receipts. The adjusted carrying amount is calculated based on the original EIR and the change in carrying amount is recorded as "Other operating income". However, for a reclassified financial asset for which the Bank subsequently increases its estimates of future cash receipts as a result of increased recoverability of those cash receipts, the effect of that increase is recognised as an adjustment to the EIR from the date of the change in estimate.

Once the recorded value of a financial asset or a group of similar financial assets has been reduced due to an impairment loss, interest income continues to be recognised using the rate of interest used to discount the future cash flows for the purpose of measuring the impairment loss.

2.3.15.2 Fee and commission income

The Bank earns fee and commission income from a diverse range of services it provides to its customers. Fee income can be divided into the following two categories:

- Fee income earned from services that are provided over a certain period of time

  Fees earned for the provision of services over a period of time are accrued over that period. These fees include commission income and asset management, custody and other management and advisory fees.

  Loan commitment fees for loans that are likely to be drawn down and other credit related fees are deferred (together with any incremental costs) and recognised as an adjustment to the EIR on the loan. When it is unlikely that a loan will be drawn down, the loan commitment fees are recognised over the commitment period on a straight-line basis.

- Fee income from providing transaction services

  Fees arising from negotiating or participating in the negotiation of a transaction for a third party, such as the arrangement of the acquisition of shares or other securities or the purchase or sale of businesses, are recognised on completion of the underlying transaction. Fees or components of fees that are linked to a certain performance are recognised after fulfilling the corresponding criteria.

2.3.15.3 Dividend income

Dividend income is recognised when the Bank's right to receive the payment is established.

2.3.15.4 Net gain/(loss) from financial instruments

Net gain/(loss) from financial investments include capital gain/(loss) from trading and fair value gain/(loss) of financial investments at fair value through profit or loss.

2.3.15.5 Other operating income

Income earned on other sources, which are not directly related to the normal operations of the Bank are recognised as other operating income on accrual basis, such as gains on disposal of property, plant and equipment and foreign exchange gain/(loss).

2.3.16 Taxes

2.3.16.1 Current tax

Current tax assets and liabilities for the current and prior years are measured at the amount expected to be recovered from or paid to the taxation authorities. The tax rates and tax laws used to compute the amount are those that are enacted or substantively enacted by the Statement of Financial Position date.

2.3.16.2 Deferred tax

Deferred tax is provided on temporary differences at the Statement of Financial Position date between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes. Deferred tax liabilities are recognised for all taxable temporary differences.

Deferred tax assets are recognised for all deductible temporary differences, carry forward of unused tax credits and unused tax losses, to the extent that it is probable that taxable profit will be available against which the deductible temporary differences, and the carry forward of unused tax credits and unused tax losses can be utilised.

The carrying amount of deferred tax assets is reviewed at each Statement of Financial Position date and reduced to the extent that it is no longer probable that sufficient taxable profit will be available to allow all or part of the deferred tax asset to be utilised. Unrecognised deferred tax assets are reassessed at each Statement of Financial Position date and are recognised to the extent that it has become probable that future taxable profit will allow the deferred tax asset to be recovered.

Deferred tax assets and liabilities are measured at the tax rates that are expected to apply in the year when the asset is realised or the liability is settled, based on tax rates (and tax laws) that have been enacted or substantively enacted at the Statement of Financial Position date.

Current tax and deferred tax relating to items recognised directly in equity are also recognised in equity and not in the Income Statement.

Deferred tax assets and deferred tax liabilities are offset if a legally enforceable right exists to set off current tax assets against current tax liabilities and the deferred taxes relate to the same taxable entity and the same taxation authority.

2.3.16.3 Value Added Tax (VAT) on financial services

VAT on financial services is calculated in accordance with the Value Added Tax Act No.14 of 2002 and subsequent amendments thereto. The base for the computation of Value Added Tax on financial services is the accounting profit before income tax adjusted for the economic depreciation and emoluments of employees' computed on prescribed rate. The VAT on financial services rate applied in 2019 is 15% (2018 – 15%).

2.3.16.4 Withholding tax on dividends

Withholding tax on dividends distributed by the Bank that arise from the distribution of dividends of the Bank is recognised at the time of liability to pay the related dividend is recognised. At present, the rate of 14% is deducted at source.

2.3.16.5 Economic Service Charge (ESC)

As per the provisions of Economic Service Charge Act No. 13 of 2006 and subsequent amendments thereto, the ESC is calculated on liable turnover. Currently, the ESC is payable at 0.5% and is deductible from the income tax payable. Unclaimed ESC, if any, can be carried forward and set-off against the income tax payable in the two subsequent years. This tax was abolished by the government with effect from 1 January 2020.

2.3.16.6 Crop Insurance Levy (CIL)

As per the provisions of the Section 14 of the Finance Act No. 12 of 2013, the CIL was introduced with effect from 1 April 2013 and is payable to the National Insurance Trust Fund. Currently, CIL is payable at 1% of the profit after tax.

2.3.16.7 Nation Building Tax (NBT) on financial services

According to the Nation Building Tax Act No. 09 of 2009 and subsequent amendments thereto, Nation Building Tax should be paid on the liable turnover with effect from 1 January 2014. NBT on financial services is calculated based on the value addition used for the purpose of VAT on financial services. The NBT rate applied up to 30 November 2019 is 2% and it was abolished with effect from 1 December 2019 (2018 – 2%).

2.3.16.8 Debts Repayments Levy (DRL)

DRL on financial services is calculated based on the total value addition used for the purpose of VAT on financial services in accordance with the Finance Act No. 35 of 2018 from 1 October 2018. The DRL rate applied in 2019 is 7% (2018 – 7%). This tax was abolished by the Government with effect from 1 January 2020.

2.3.17 Grants

Grants are recognised where there is reasonable assurance that the grant will be received and all attached conditions will be complied with. When the grant relates to an expense item, it is recognised as income over the period necessary to match the grant on a systematic basis to the costs that it is intended to compensate. When the grant relates to an asset, it is recognised as deferred income and released to income in equal amounts over the expected useful life of the related asset.

2.3.18 Dividends on ordinary shares

Dividends on ordinary shares are recognised as a liability and deducted from equity when they are approved by the Bank's shareholders. Interim dividends are deducted from equity when they are declared and no longer at the discretion of the Bank.

Dividends for the year that are approved after the Statement of Financial Position date are disclosed as an event after the reporting date.

2.3.19 Equity reserves

The reserves recorded in equity on the Bank's Statement of Financial Position include:

"Available-for-sale/fair value through OCI" reserve which comprises changes in fair value of fair value through other comprehensive income investments.

2.3.20 Segment reporting

A segment is a distinguishable component of the Bank that is engaged in providing services (Business segments) or in providing services within a particular economic environment (Geographical segment) which is subject to risks and rewards that are different from those of other segments.

In accordance with the SLFRS 8 on "Segmental Reporting", segmental information is presented in respect of the Bank based on Bank's Management and internal reporting structure.

The Bank's segmental reporting is based on the following operating segments.

Banking	:	Individual customers' deposits and consumer financing, equipment financing, home and property financing
Leasing	:	Lease and hire purchase facility customers
Treasury	:	Placements of funds with other banks and financial institutions, equity investments
Pawning	:	Pawning advances to customers

Management monitors the operating results of its business units separately for the purpose of making decisions about resource allocation and performance assessment. Segment performance is evaluated based on operating profit or loss of respective segment.

2.4 Sri Lanka Accounting Standards not yet effective as at 31 December 2019

The following Sri Lanka Accounting Standards and interpretations have been issued by The Institute of Chartered Accountants of Sri Lanka which are not yet effective as at 31 December 2019. The Bank intends to adopt these new and amended standards, if applicable, when they become effective.

SLFRS 17 – Insurance contracts

SLFRS 17 "Insurance Contracts", is a comprehensive new accounting standard for insurance contracts covering recognition and measurement, presentation and disclosures. Once effective, SLFRS 17 replaces existing SLFRS 4 "Insurance contracts". The overall objective of SLFRS 17 is to provide an accounting model for insurance contracts that is more useful and consistent for insurers.

SLFRS 17 is effective for reporting periods beginning on or after 1 January 2021. Early application permitted, if the entity is applying SLFRS 16 and SLFRS 15 on or before the date in which it first applies SLFRS 17. This standard is not applicable to the Bank.

Amendments to LKAS 1 and LKAS 8: Definition of material

Amendments to LKAS 1 "Presentation of Financial Statements" and LKAS 8 "Accounting policies, Changes in accounting Estimates and Errors" are made to align the definition of "material" across the standard and to clarify certain aspects of the definition. The new definition states that, "information is material if omitting or obscuring it could reasonably be expected to influence decisions that the primary users of general purpose financial statements make on the basis of those financial statements, which provide financial information about a specific reporting entity".

The amendments are applied prospectively for the annual periods beginning on or after 1 January 2020 with early application permitted.

The amendments to the definition of material are not expected to have a significant impact on the Bank's Financial Statements.

Amendments to SLFRS 3: Definition of a business

Amendments to the definition of a business in SLFRS 3 "Business Combinations" are made to help the entities determine whether an acquired set of activities and assets is a business or not. They clarify the minimum requirements for a business, remove the assessment of whether market participants are capable of replacing any missing elements, add guidance to help entities assess whether an acquired process is substantive, narrow the definition of a business and of outputs, and introduce an optional fair value concentration test.

Since the amendments are applied prospectively to all business combinations and asset acquisitions for which the acquisition date is on or after the first annual reporting period beginning on or after 1 January 2020 with early application permitted.

Amendments to references to the conceptual framework in SLFRS standards

Revisions to the Conceptual Framework were made because some important issues were not covered and some guidance was unclear or out of date. The revised Conceptual Framework includes:

- a new chapter on measurement;
- guidance on reporting financial performance;
- improved definitions of an asset and a liability, and guidance supporting these definitions; and
- clarifications in important areas, such as the roles of stewardship, prudence and measurement uncertainty in financial reporting

Since the amendments are effective for annual periods beginning on or after 1 January 2020, the Bank will not be affected by these amendments as at the reporting date. Further, the amendments to the references to the conceptual framework in SLFRS standards are not expected to have a significant impact on the Bank's Financial Statements.

For the year ended 31 December

3 Net interest income

	2019 LKR	2018 LKR
Interest income		
Cash and cash equivalents	89,311,724	60,099,522
Placements with banks	760,109,685	851,002,417
Financial assets at amortised cost		
– Loans and receivables to other customers*	13,839,972,079	11,985,315,386
– Debt and other instruments	389,930,319	250,369,831
Total interest income	15,079,323,806	13,146,787,156
Interest expenses		
Financial liabilities at amortised cost		
– Due to other customers	7,051,780,733	6,576,577,677
– Due to debt securities holders	98,141,850	393,858,241
– Other borrowers	2,189,361,846	1,453,321,810
– Finance cost of lease liability	43,244,491	–
Total interest expenses	9,382,528,920	8,423,757,728
Net interest income	5,696,794,886	4,723,029,428

** Late fee charged from overdue rentals classified under net fee and commission income in 31 December 2018 has been reclassified to interest income and comparative figure in this Financial Statement is amended. (Refer Note 44)*

3.1 Net interest income from Sri Lanka Government Securities

	2019 LKR	2018 LKR
Net interest income from Sri Lanka Government Securities	325,074,604	149,604,115
Total	325,074,604	149,604,115

4 Net fee and commission income

	2019 LKR	2018 LKR
Fee and commission income*	237,656,461	196,762,071
Fee and commission expenses	(6,506,626)	(4,396,881)
Net fee and commission income	231,149,835	192,365,190

4.1 Net fee and commission earned from

	2019 LKR	2018 LKR
Loans	128,412,167	98,983,799
Deposits	1,591,602	1,629,265
Guarantees	1,885,322	2,232,754
Commission earned from insurance	21,692,391	18,776,277
Commission earned from ATM	17,724,505	18,652,403
Others	59,843,848	52,090,692
Net fee and commission income	231,149,835	192,365,190

** Late fee charged from overdue rentals classified under net fee and commission income in 31 December 2018 has been reclassified to interest income and comparative figure in this Financial Statement is amended. (Refer Note 44)*

For the year ended 31 December

5 Net fair value gain/(loss) from financial assets at fair value through profit or loss

	2019 LKR	2018 LKR
Sri Lanka Government Securities – Treasury bills	(58,050)	(942,414)
Unit Trust	114,947,499	281,114,474
Total	**114,889,449**	280,172,060

6 Net other operating income

	2019 LKR	2018 LKR
Gain on sale of property, plant and equipment	12,055,221	2,812,163
Dividend income	240,800	476,587
Account maintenance fees	75,675,472	16,329,296
Other income	2,997,292	1,193,056
Other operating income	**90,968,785**	20,811,102

7 Impairment for loans and other losses

7.1 Balance with Bank

	2019 LKR	2018 LKR
Stage 1	(267,938)	606,166
Total	**(267,938)**	606,166

7.2 Placement with banks

	2019 LKR	2018 LKR
Stage 1	(4,848,662)	5,671,770
Total	**(4,848,662)**	5,671,770

7.3 Financial assets at amortised cost – Loans and receivables to customers

	2019 LKR	2018 LKR
Stage 1	231,986,335	(9,390,783)
Stage 2	(105,851,634)	48,205,067
Stage 3	795,892,983	480,902,288
Total	**922,027,684**	519,716,573

7.4 Debt and other instruments

	2019 LKR	2018 LKR
Stage 1	522,422	(150,628)
Total	**522,422**	(150,628)
Total	**917,433,506**	525,843,881

For the year ended 31 December

8 Personnel expenses

	2019 LKR	2018 LKR
Salary and bonus	**1,518,776,089**	1,343,605,896
Contributions to defined contribution plans – EPF	**202,665,907**	178,360,466
– ETF	**43,427,993**	38,216,904
Contributions to defined benefit plans	**92,127,811**	54,590,639
Overtime	**7,282,232**	7,932,044
Staff welfare	**29,112,351**	26,607,544
Staff allowances	**104,383,718**	78,858,344
Others	**118,571,829**	98,901,512
Total	**2,116,347,930**	1,827,073,349

9 Depreciation and amortisation expenses

	2019 LKR	2018 LKR
Depreciation of property, plant and equipment	**228,739,345**	218,783,787
Amortisation of Right of use assets	**182,256,972**	–
Depreciation of investment property	**1,056,030**	1,056,030
Amortisation of intangible assets	**19,140,249**	4,420,615
Total	**431,192,597**	224,260,432

10 Other expenses

	2019 LKR	2018 LKR
Directors' emoluments	**22,346,444**	19,660,000
Auditors' remunerations	**4,195,864**	4,000,000
Professional and legal expenses	**6,752,497**	1,495,216
Office administration and establishment expenses	**1,386,778,240**	1,500,976,636
Total	**1,420,073,045**	1,526,131,852

10.1 Directors' emoluments include fees paid to Non-executive Directors.

11 Tax expense

	2019 LKR	2018 LKR
Current tax expense		
Income tax for the year	**452,640,558**	341,234,017
Adjustment in respect of current income tax of prior periods	**31,203,942**	46,084,930
Deferred taxation charge/(reversal)	**(151,422,156)**	(100,126,593)
Total	**332,422,344**	287,192,354

For the year ended 31 December

11.1 Reconciliation of tax expenses

	2019 LKR	2018 LKR
Profit before tax	585,827,440	644,142,473
Income tax for the period (Accounting profit @ 28%)	164,031,683	180,359,893
Income exempt from tax/or not taxable	(3,442,886)	(36,886,787)
Adjustment in respect of current income tax of prior periods	31,203,942	46,084,930
Add: Tax effect of expenses that are not deductible for tax purposes	538,933,025	778,552,158
Less: Tax effect of expenses that are deductible for tax purposes	(288,309,630)	(520,532,902)
Add: Tax impact on leasing loss	41,428,366	(60,258,345)
Tax expense for the period	483,844,500	387,318,947
Deferred taxation charge	(151,422,156)	(100,126,593)
At the effective income tax rate of 56.74% (2018: 44.59%)	332,422,344	287,192,354

11.2 Deferred tax assets, liabilities and income tax relates to the followings:

	Statement of financial position		Statement of comprehensive income	
	2019 LKR	2018 LKR	2019 LKR	2018 LKR
Deferred tax liability				
Capital allowances for property, plant and equipment	50,479,669	15,637,704	34,841,965	(8,370,430)
Capital allowances for leased assets	100,495,732	148,218,327	(47,722,595)	(37,009,763)
	150,975,401	163,856,031	(12,880,630)	(45,380,193)
Deferred tax assets				
Defined benefit plans	131,762,557	99,359,246	(32,403,311)	(27,358,202)
Loss on lease assets	–	–	–	79,234,788
Impairment allowance	244,367,815	133,911,711	(110,456,104)	(133,911,711)
Right to use assets	7,326,690	–	(7,326,690)	–
	383,457,062	233,270,957	(150,186,105)	(82,035,125)
Deferred taxation charge/(reversal)			(163,066,735)	(127,415,319)
Net deferred tax liability/assets	(232,481,661)	(69,414,926)		

11.2.1 Composition of deferred tax charge

	2019 LKR	2018 LKR
Impact on income tax expense	(151,422,156)	(100,126,593)
Impact on other comprehensive income	(11,644,579)	(12,878,686)
Impact on comprehensive income	(163,066,735)	(113,005,279)
Impact on opening balance under SLFRS 09	–	(14,410,040)
Total impact	(163,066,735)	(127,415,319)

12 *Earnings per share*

Basic earnings per share amounts are calculated by dividing the net profit for the year attributable to ordinary shareholders (after deducting preference share dividends, if any) by the weighted average number of ordinary shares outstanding during the year. The weighted average number of ordinary shares outstanding during the year and the previous year are adjusted for events that have changed the number of ordinary shares outstanding, without a corresponding change in the resources such as a scrip dividend.

	2019 LKR	2018 LKR
Net profit for the period	253,405,096	356,950,119
Profit attributable to ordinary shareholders	253,405,096	356,950,119

	2019 Number	2018 Number
Weighted average number of ordinary shares in issue	56,308,252	56,308,252
	56,308,252	56,308,252
Basic/diluted earnings per ordinary share	4.50	6.34

The subordinated term debts detailed in Note 27 are resulted for anti-diluted earnings per share.

13 *Cash and cash equivalents*

	2019 LKR	2018 LKR
Cash in hand	272,317,628	424,829,523
Balances with banks	2,157,826,360	3,747,730,463
Less : Impairment	(353,418)	(621,356)
Carrying value after impairment	2,429,790,570	4,171,938,630

13.1 Analysis of cash and cash equivalents based on exposure to credit risk

	Stage 1	
	2019 LKR	2018 LKR
Placements	2,430,143,988	4,172,559,986
Less: Impairment	(353,418)	(621,356)
Carrying value after impairment	2,429,790,570	4,171,938,630

13.2 Stage wise classification of impairment allowances of cash and cash equivalents

	Stage 1	
	2019 LKR	2018 LKR
Opening balance as at 1 January	621,356	15,190
Charges/(write back) to income statement	(267,938)	606,166
Closing balance as at 31 December	353,418	621,356

For the year ended 31 December

13.3 Cash and cash equivalents for cash flow statement

	2019 LKR	2018 LKR
Cash and cash equivalents	2,429,790,570	4,171,938,630
Repurchase agreement	4,332,653,659	2,934,221,630
Fixed deposits less than 3 months	4,152,234,452	9,509,742,123
Total	10,914,678,681	16,615,902,383

14 Placements with banks

	2019 LKR	2018 LKR
Placements with Banks	5,630,717,976	9,535,897,658
Less: Impairment	(2,623,431)	(7,472,093)
Carrying value after impairment	5,628,094,545	9,528,425,565

14.1 Analysis of placements with banks based on exposure to credit risk

	Stage 1	
	2019 LKR	2018 LKR
Placements with banks	5,630,717,976	9,535,897,658
Less: Impairment allowance for placement	(2,623,431)	(7,472,093)
Carrying value after impairment	5,628,094,545	9,528,425,565

14.2 Stage wise classification of impairment allowances of placements with banks

	Stage 1	
	2019 LKR	2018 LKR
Opening balance as at 1 January	7,472,093	1,800,323
Charges/(write back) to income statement	(4,848,662)	5,671,770
Closing balance as at 31 December	2,623,431	7,472,093

15 Financial assets at fair value through profit or loss

	2019 LKR	2018 LKR
Sri Lanka Government Securities – Treasury bills	46,519,350	–
Unit Trust	3,480,790,791	146,103,330
Total	3,527,310,141	146,103,330

16 Financial assets at amortised cost – Loans and receivables to other customers

	2019 LKR	2018 LKR
Gross loans and receivables (16.1)	88,720,800,911	79,482,459,527
Less: Individual impairment	(891,669,149)	(350,360,455)
Collective impairment	(2,005,796,900)	(1,625,077,910)
Net loans and receivables	85,823,334,862	77,507,021,162

For the year ended 31 December

16.1 Analysis of loans and receivables to other customers based on exposure to credit risk

	2019			
	Stage 1 LKR	Stage 2 LKR	Stage 3 LKR	Total LKR
Significant impairment loans				
Term loan	–	–	2,429,448,220	2,429,448,220
Leasing	–	–	347,461,848	347,461,848
Collective impairment loans				
Pawning	1,659,484,155	30,675,731	22,012,069	1,712,171,954
Cash margin	4,645,118,340	793,272,466	4,963,166	5,443,353,971
Staff loans	1,252,923,774	4,610,333	22,812,160	1,280,346,267
Term loans				
Business	10,338,753,420	238,259,107	898,766,510	11,475,779,037
Co-operative	2,100,930,848	101,685,565	82,598,336	2,285,214,749
Housing	2,638,550,309	456,060,240	221,438,389	3,316,048,938
Personal	51,175,819,323	923,660,778	1,888,639,373	53,988,119,475
Lease rentals receivables	4,398,092,872	1,774,794,840	269,968,740	6,442,856,452
Gross loans and receivables	78,209,673,042	4,323,019,060	6,188,108,809	88,720,800,911
Less: Impairment allowance	(550,264,452)	(163,953,856)	(2,183,247,741)	(2,897,466,049)
Net loans and receivables	77,659,408,590	4,159,065,203	4,004,861,069	85,823,334,862

	2018			
	Stage 1 LKR	Stage 2 LKR	Stage 3 LKR	Total LKR
Significant impairment loans				
Term loan	–	–	1,000,469,342	1,000,469,342
Leasing	–	–	145,961,745	145,961,745
Collective impairment loans				
Pawning	1,187,539,873	56,887,961	13,850,772	1,258,278,606
Cash margin	5,134,496,941	430,882,184	8,813,039	5,574,192,164
Staff loans	1,097,737,911	–	23,866,152	1,121,604,063
Term loans				
Business	7,763,492,734	1,161,498,837	595,625,756	9,520,617,327
Co-operative	2,133,338,868	111,133,683	287,054,035	2,531,526,586
Housing	2,200,895,413	453,150,141	240,483,984	2,894,529,538
Personal	47,665,057,056	1,126,826,518	1,553,195,979	50,345,079,553
Lease rentals receivables	3,562,166,844	1,295,727,450	232,306,309	5,090,200,603
Gross loans and receivables	70,744,725,640	4,636,106,774	4,101,627,113	79,482,459,527
Less: Impairment allowance	(318,278,117)	(269,805,490)	(1,387,354,758)	(1,975,438,365)
Net loans and receivables	70,426,447,523	4,366,301,284	2,714,272,355	77,507,021,162

For the year ended 31 December

16.2 Gross loans and receivables analysis by product

	2019 LKR	2018 LKR
Loans and receivables		
Pawning	1,712,171,954	1,258,278,606
Cash margin	5,443,353,971	5,574,192,164
Staff loans	1,280,346,267	1,121,604,063
Lease rentals receivable (Note 16.2.1)	6,790,318,300	5,236,162,349
Term loans		
Business	13,255,022,223	10,248,947,436
Co-operative	2,775,250,944	2,682,172,444
Housing	3,416,424,007	2,971,196,180
Personal	54,047,913,244	50,389,906,285
Gross total	88,720,800,911	79,482,459,527

16.2.1 Lease rentals receivable

	2019 LKR	2018 LKR
Within one year	3,202,575,288	2,896,844,537
One to five years	5,177,577,345	3,890,404,144
After five years	–	35,539,483
– Unearned income on rentals receivable	(1,589,834,333)	(1,586,625,815)
	6,790,318,300	5,236,162,349

16.3 Gross loans and receivables analysis by currency

	2019 LKR	2018 LKR
Sri Lankan Rupee	88,720,800,911	79,482,459,527
Gross total	88,720,800,911	79,482,459,527

16.4 Analysis of loans and receivables to other customers based on exposure to credit risk

	2019 LKR	2018 LKR
Stage 1		
Opening balance as at 1 January	318,278,117	327,668,900
Charges/(write back) to income statement	231,986,335	(9,390,783)
Closing balance as at 31 December	550,264,452	318,278,117
Stage 2		
Opening balance as at 1 January	269,805,490	221,600,423
Charges/(write back) to income statement	(105,851,634)	48,205,067
Closing balance as at 31 December	163,953,856	269,805,490
Stage 3		
Opening balance as at 1 January	1,387,354,758	917,503,123
Charges/(write back) to income statement	795,892,983	480,902,288
Write-off during the year	–	(11,050,653)
Closing balance as at 31 December	2,183,247,741	1,387,354,758

For the year ended 31 December

16.5 Movement in individual and collective impairment

	Individual impairment LKR	Collective impairment LKR	Total Impairment LKR
Restated balance under SLFRS 9 as at 1 January 2018	220,946,259	1,245,826,188	1,466,772,447
Charge/(write back) to income statement	129,414,196	390,302,377	519,716,573
Recovery/(write-off) during the year	–	(11,050,655)	(11,050,655)
Closing balance as at 31 December 2018	350,360,455	1,625,077,910	1,975,438,365
Opening balance as at 1 January 2019	350,360,455	1,625,077,910	1,975,438,365
Charge/(write back) to income statement	541,308,694	380,718,990	922,027,684
Recovery/(write-off) during the year	–	–	–
Closing balance as at 31 December 2019	891,669,149	2,005,796,900	2,897,466,049

17 Financial assets at amortised cost – Debt and other instruments

	2019 LKR	2018 LKR
Debentures	**93,473,535**	174,804,870
Repurchase agreement	**4,332,653,659**	2,934,221,630
Treasury bill	**1,771,722,268**	296,755,397
Commercial papers	**801,779,452**	–
Less: Impairment	**(704,033)**	(181,611)
Carrying value after impairment	**6,998,924,881**	3,405,600,286

17.1 Analysis of debt and other instruments based on exposure to credit risk

	Stage 1	
	2019 LKR	2018 LKR
Debentures	**93,473,535**	174,804,870
Repurchase agreement	**4,332,653,659**	2,934,221,630
Treasury bill	**1,771,722,268**	296,755,397
Commercial papers	**801,779,452**	–
Less: Impairment allowance	**(704,033)**	(181,611)
Carrying value after impairment	**6,998,924,881**	3,405,600,286

17.2 Stage wise classification of impairment allowances of debt and other instruments

	Stage 1	
	2019 LKR	2018 LKR
Opening balance as at 1 January	**181,611**	332,239
Charges/(write back) to income statement	**522,422**	(150,628)
Closing balance as at 31 December	**704,033**	181,611

18 Financial assets measured at fair value through other comprehensive income

	2019 LKR	2018 LKR
Unquoted equity securities (Note 18.1)	56,938,514	60,148,048
Financial assets measured at fair value through other comprehensive income	56,938,514	60,148,048

18.1 Unquoted equity securities

	2019		2018	
	Number of shares	Amount LKR	Number of shares	Amount LKR
SANASA Insurance Company Limited	7,590,494	75,904,944	7,590,494	75,904,944
Credit Information Bureau of Sri Lanka	100	10,000	100	10,000
Consorzio Etimos S.C.	2	75,194	2	75,194
Loss from mark to market valuation as at 31 December market value		(19,051,624)		(15,842,090)
		56,938,514		60,148,048

18.1.1 Movement in unquoted equity securities

	2019 LKR	2018 LKR
Opening Balance as at 1 January	60,148,048	63,536,159
Investments made during the year	–	–
Disposal during the year	–	–
Loss from mark to market valuation	(3,209,534)	(3,388,111)
Closing balance as at 31 December	56,938,514	60,148,048

18.1.2 Valuation of unquoted equity securities

Type	Level	Method of valuation	Significant unobservable inputs	Sensitivity of fair value to unobservable inputs
Unquoted share investment	Level 3	Market approach – Price to book value of comparable peer companies	Medium price to book value – liquidity discount	Positively correlated sensitivity
			Regulatory non-compliance adjustment	Positively correlated sensitivity

19 Property, plant and equipment

2019	Land and buildings LKR	Leasehold properties LKR	Computer hardware LKR	Machinery and equipment LKR	Furniture and fittings LKR	Motor vehicles LKR	Total LKR
Cost							
Opening balance as at 1 January 2019	251,979,214	590,000	770,392,814	502,015,293	375,412,047	155,821,731	2,056,211,099
Additions	–	–	70,837,633	33,733,536	42,058,542	25,015,227	171,644,938
Disposals	–	(590,000)	(7,901,370)	(8,085,296)	(17,798,119)	(18,030,805)	(52,405,590)
Closing balance as at 31 December 2019	251,979,214	–	833,329,077	527,663,533	399,672,470	162,806,153	2,175,450,447
Less: Accumulated depreciation							
Opening balance as at 1 January 2019	31,597,097	590,000	578,596,828	394,948,782	222,178,506	123,561,393	1,351,472,606
Charge for the year	3,873,373	–	108,488,036	44,865,376	53,138,582	18,373,979	228,739,345
Disposals	–	(590,000)	(7,901,370)	(7,293,641)	(17,101,672)	(17,106,267)	(49,992,949)
Closing balance as at 31 December 2019	35,470,471	–	679,183,494	432,520,517	258,215,416	124,829,105	1,530,219,002

For the year ended 31 December

2018	Land and buildings LKR	Leasehold properties LKR	Computer hardware LKR	Machinery and equipment LKR	Furniture and fittings LKR	Motor vehicles LKR	Total LKR
Cost							
Opening balance as at 1 January 2018	251,979,214	590,000	678,783,946	480,614,783	325,426,778	145,774,508	1,883,169,229
Additions	–	–	104,758,145	33,466,175	66,557,679	12,152,546	216,934,546
Disposals	–	–	(13,149,277)	(12,065,666)	(16,572,410)	(2,105,323)	(43,892,676)
Closing balance as at 31 December 2018	251,979,214	590,000	770,392,814	502,015,293	375,412,047	155,821,731	2,056,211,099
Less: Accumulated depreciation							
Opening balance as at 1 January 2018	29,721,712	590,000	481,626,273	363,356,943	194,351,555	104,837,167	1,174,483,649
Charge for the year	1,875,385	–	109,850,005	42,348,288	43,880,560	20,829,549	218,783,787
Disposals	–	–	(12,879,450)	(10,756,449)	(16,053,609)	(2,105,323)	(41,794,831)
Closing balance as at 31 December 2018	31,597,097	590,000	578,596,828	394,948,782	222,178,506	123,561,393	1,351,472,605

	Land and buildings LKR	Leasehold properties LKR	Computer hardware LKR	Machinery and equipment LKR	Furniture and fittings LKR	Motor vehicles LKR	Total LKR
Net book value as at 31 December 2019	216,508,744	–	154,145,583	95,143,016	141,457,054	37,977,048	645,231,444
Net book value as at 31 December 2018	220,382,118	–	191,795,986	107,066,511	153,233,541	32,260,338	704,738,493

19.1 Freehold land and buildings

The details of the Land and Buildings owned by the Bank are as follows:

Location/Address	Extent		As at 31 December 2019		As at 31 December 2018	
			Cost		Cost	
	Land (Purchase)	Building (Square feet)	Land LKR	Building LKR	Land LKR	Building LKR
No. 14, Edmonton Road, Kirulapone	17.85	–	38,999,000	–	38,999,000	–
No. 12/01, Edmonton Road, Kirulapone	18.05	–	46,799,000	–	46,799,000	–
A1, SANASA Housing Project, Toppass, Nuwara Eliya	14	1,200	400,000	2,100,000	400,000	2,100,000
No. 145, Rathnapura Road, Horana	13	5,956	20,539,000	6,500,000	20,539,000	6,500,000
No. 63A, Matara Road, Akuressa	14	3,728	14,423,820	8,975,180	14,423,820	8,975,180
No. 255, Sunnysaid Garden, Karapitiya	18.50	5,992	9,250,000	20,833,360	9,250,000	20,833,360
No. 342, Main Street, Kegalle	13.25	5,580	34,760,400	14,118,600	34,760,400	14,118,600
No. 6/176, Walauwatta, Kegalle	20	–	16,639,000	–	16,639,000	–
No. 5/176, Walauwatta, Kegalle	12	1,334	8,400,000	1,250,000	8,400,000	1,250,000
SANASA Campus Ltd, Paragammana, Hettimulla, Kegalle	320	2,600	1,002,912	4,568,824	1,002,912	4,568,824
60/65, Sahasapura Scheme, Baseline Mawatha, Borella	–	1,006	–	2,420,118	–	2,420,118
			191,213,132	60,766,082	191,213,132	60,766,082

19.2 During the financial year, the Bank acquired property, plant and equipment to the aggregate value of LKR 171,644,940/- (2018 – LKR 216,934,546/-). Cash payments amounting to LKR 171,644,940/- (2018 – LKR 216,934,546/-) were made during the year for purchase of property, plant and equipment.

19.3 Property, plant and equipment includes fully depreciated assets having a gross carrying amounts of LKR 1,267,939,427/- (2018 – LKR 1,040,724,692/-)

19.4 There were no restrictions on the title of the property, plant and equipment as at 31 December 2019.

19.5 There were no idle property, plant and equipment as at 31 December 2019.

20 Right of use assets

	2019 LKR	2018 LKR
Opening balance as at 1 January	–	–
Present value of the lease payments	481,376,365	–
Prepayment	104,348,737	–
Effect of adoption of SLFRS 16 as at 1 January 2019	585,725,102	–
Additions and improvements during the year	247,802,618	–
Amortisation expenses for the year	(182,256,972)	–
Net book value as at 31 December	**651,270,748**	–

21 Investment properties

	2019 LKR	2018 LKR
Cost		
Opening balance as at 1 January	35,359,000	35,359,000
Additions	–	–
Closing balance as at 31 December	35,359,000	35,359,000
Less: Accumulated depreciation		
Opening balance as at 1 January	13,024,370	11,968,340
Charge for the year	1,056,030	1,056,030
Closing balance as at 31 December	14,080,400	13,024,370
Net book value as at 31 December	**21,278,600**	22,334,630

21.1 The details of the investment properties owned by the Bank are as follows:

	Extent		31 December 2019 Cost		31 December 2018 Cost	
Location/Address	Land (Purchase)	Building (Square feet)	Land LKR	Building LKR	Land LKR	Building LKR
No. 6 A/176, Walauwatta, Kegalle	28	8,233.5	14,238,400	21,120,600	14,238,400	21,120,600
			14,238,400	21,120,600	14,238,400	21,120,600

21.2 There were no direct operating expenses arising from investment property that generated retain income and that did not generate material rental income.

21.3 Assets classified as investment properties include land and building located in kegalle. Market value (Level 3) of the above asset is LKR 52,788,900/- . Valuation was carried out by R M W N K Chandrasekara independendent Professional Valuer.

22 Intangible assets

	2019 LKR	2018 LKR
Cost		
Opening balance as at 1 January	211,929,704	211,929,704
Additions	323,857,065	–
Closing balance as at 31 December	535,786,769	211,929,704
Less: Accumulated amortisation		
Opening balance as at 1 January	208,201,979	203,781,364
Charge for the year	19,140,249	4,420,615
Closing balance as at 31 December	227,342,228	208,201,979
Net book value as at 31 December	308,444,541	3,727,725

22.1 There were no idle Intangible assets as at 31 December 2019.

22.2 There were no restrictions on the title of the intangible assets as at 31 December 2019.

23 Other assets

	2019 LKR	2018 LKR
Postage legal and other charges receivable	74,976,255	55,628,494
VAT receivable	–	7,314,404
Prepaid staff cost	718,181,850	635,701,610
Deposits and prepayments	586,153,879	425,178,412
Inventory	81,211,838	74,491,470
Total	1,460,523,822	1,198,314,390

24 Due to other customers

	2019 LKR	2018 LKR
Total amount due to other customers	72,431,923,465	67,474,821,535
Total	72,431,923,465	67,474,821,535

24.1 Analysis of due to other customers

	2019 LKR	2018 LKR
By product		
Savings deposits	15,540,255,346	12,369,442,964
Fixed deposits	56,891,668,119	55,105,378,571
Total	72,431,923,465	67,474,821,535

	2019 LKR	2018 LKR
By currency		
Sri Lanka Rupee	72,431,923,465	67,474,821,535
Total	72,431,923,465	67,474,821,535

25 Other borrowings

	2019 LKR	2018 LKR
Term loan (Note 25.1)	16,735,146,458	12,347,696,633
Securitised borrowings (Note 25.2)	1,322,982,880	827,867,887
Refinance borrowing (Note 25.3)	2,241,588,630	2,245,403,442
Total	20,299,717,968	15,420,967,962

25.1 Details of term loans

Institution	Fixed/Floating	Tenure (Months)	2019 LKR	2018 LKR
National Savings Bank	Floating	48	207,769,764	458,077,389
National Savings Bank	Floating	48	1,332,800,000	1,833,200,000
Sampath Bank PLC	Floating	60	58,409,645	158,658,090
Sampath Bank PLC	Floating	60	58,409,645	158,658,090
Sampath Bank PLC	Floating	60	200,375,404	300,675,854
Sampath Bank PLC	Floating	60	217,076,694	317,382,295
Sampath Bank PLC	Floating	60	1,870,318,174	–
Seylan Bank PLC	Floating	48	407,168,242	38,094,448
Seylan Bank PLC	Floating	60	617,216,681	823,023,219
Seylan Bank PLC	Floating	48	810,352,488	–
Seylan Bank PLC	Floating	60	1,003,945,205	–
Seylan Bank PLC	Floating	60	501,972,603	–
DFCC Bank	Floating	48	323,578,596	489,776,081
DFCC Bank	Floating	48	364,832,444	448,974,730
Peoples Bank	Floating	60	357,154,938	786,169,108
Peoples Bank	Floating	3	504,238,356	–
Peoples Bank	Floating	3	500,160,137	–
MCB Bank Ltd	Floating	60	91,379,307	141,502,782
HNB Bank PLC	Floating	48	313,329,431	564,330,767
HNB Bank PLC	Floating	48	1,094,441,610	1,469,852,568
NDB Bank PLC	Fixed/Floating	–	–	1,013,227,397
NDB Bank PLC	Floating	1	150,749,589	–
NDB Bank PLC	Floating	1	301,499,178	–
NDB Bank PLC	Floating	1	150,562,192	–
NDB Bank PLC	Floating	1	100,374,795	–
NDB Bank PLC	Floating	1	300,090,411	–
Bank of Ceylon	Floating	60	1,403,234,192	–
Nations Trust Bank PLC	Floating	48	940,066,488	–
The International Finance Corporation (IFC)	Fixed	60	1,889,186,294	2,415,304,500
The Netherlands Development Finance Company (FMO)	Floating	52	664,453,956	930,789,315
			16,735,146,458	12,347,696,633

For the year ended 31 December

25.1.1 Movement in term loans

	Opening balance as at 1 January 2019 LKR	Obtained during year LKR	Repayment LKR	Closing balance as at 31 December 2019 LKR
National Savings Bank	2,291,100,000	–	(750,600,000)	**1,540,500,000**
Sampath Bank PLC	933,248,000	2,000,000,000	(533,365,333)	**2,399,882,667**
Seylan Bank PLC	859,050,000	3,000,000,000	(528,424,994)	**3,330,625,006**
Peoples Bank	781,547,486	3,000,000,000	(2,426,298,629)	**1,355,248,857**
MCB Bank Ltd	141,450,000	–	(50,100,000)	**91,350,000**
HNB Bank PLC	2,031,320,000	–	(624,960,000)	**1,406,360,000**
NDB Bank PLC	1,000,000,000	7,950,000,000	(7,950,000,000)	**1,000,000,000**
DFCC Bank	937,499,998	–	(250,000,008)	**687,499,990**
Bank of Ceylon	–	1,400,000,000	–	**1,400,000,000**
Nations Trust Bank	–	1,000,000,000	(62,502,000)	**937,498,000**
FMO	925,530,757	–	(264,437,359)	**661,093,398**
IFC	2,331,000,000	–	(517,999,995)	**1,813,000,005**
Interest Payable	115,950,393	–	–	**112,088,534**
	12,347,696,633	18,350,000,000	(13,958,688,318)	**16,735,146,458**

25.2 Securitised borrowings

	2019 LKR	2018 LKR
Trust 1	**–**	4,269,292
Trust 2	**373,969,439**	823,598,595
Trust 3	**949,013,441**	–
Total	**1,322,982,880**	827,867,887

25.3 Refinance borrowings

	2019 LKR	2018 LKR
SANASA Federation (Refinance of *Athwela* Loans)	**54,200,000**	54,200,000
Central Bank of Sri Lanka (RERED)	**–**	3,930,019
Central Bank of Sri Lanka (*Susahana*)	**80,827**	80,827
Asian Development Bank (*Dasuna*)	**19,658**	191,488
Borrowings under CBSL – Tea Development	**–**	103,530
Borrowings under Refinance of *Jayatha*	**475,435,470**	441,306,600
Borrowing under Awakaning East	**–**	30,123,850
Borrowing under Awakaning North	**145,825**	1,671,750
Borrowing under *Saubagya*	**1,231,893,619**	1,246,363,283
Borrowing under SPENDP	**72,000**	408,000
Borrowing – Refinance Smile iii	**439,890,700**	434,120,501
Borrowing – Refinance Sepi	**1,900,000**	2,700,000
Borrowing – *Suwashakthi* Loan	**2,616,328**	3,848,997
Borrowing – *Athwela* (READ)	**21,118,334**	25,516,667
Borrowing – *Kapruka Ayojana*	**14,215,870**	837,930
	2,241,588,630	2,245,403,442

25.4 Maturity analysis of refinance borrowings

	2019 LKR	2018 LKR
Due within one year	845,552,922	985,193,182
1-5 years	1,377,200,599	1,223,230,860
After 5 years	18,705,800	36,979,400
Total	2,241,459,321	2,245,403,442

25.5 Securities and terms of borrowings

Interest rate ranging for above borrowings 0% to 13.75% per annum.

Bank has pledged from the lease portfolio sum of LKR 1,222,145,124/- for the securitised borrowings (2018 – LKR 1,892,536,930/-).

26 Debt security issued

	2019 LKR	2018 LKR
Debentures	1,014,034,248	4,198,547,716
Total	1,014,034,248	4,198,547,716

26.1 Types of debentures (Fixed)

(i) Rated Guaranteed Redeemable Debentures of LKR 100 each – Guaranteed by Sampath Bank PLC. The debentures are quoted on the Colombo Stock Exchange. (Rated (SL)A+ (SO) with a Stable Outlook by ICRA Lanka Limited)

Type	Interest payable frequency	Issue date	Maturity date	Annual effective rate (AER) %	Face value LKR	Interest payable LKR	Balance LKR
B	Semi Annually	31 December 2015	31 December 2020	10.25	402,610,000	20,295,956	422,905,956

(ii) Rated Guaranteed Redeemable Debentures of LKR 100 each – Guaranteed by Seylan Bank PLC. The debentures are quoted on the Colombo Stock Exchange. (Rated (SL)A- (SO) with a Stable Outlook by ICRA Lanka Limited)

Type	Interest payable frequency	Issue date	Maturity date	Annual effective rate (AER) %	Face value LKR	Interest payable LKR	Balance LKR
D	Semi Annually	31 December 2015	31 December 2020	10.57	561,950,000	29,178,292	591,128,292
					964,560,000	49,474,248	1,014,034,248

27 Subordinated term debts

	2019 LKR	2018 LKR
Subordinated term debts	4,210,565,525	1,008,027,823
Total	4,210,565,525	1,008,027,823

For the year ended 31 December

27.1 Details of subordinated term debts

Investor	Tenor/Repayment	Interest Rate	2019 LKR	2018 LKR
FMO	Repayment or conversion after 66 months	6-month T-bill rate + 550 basis points Payable per annum	316,124,625	316,696,269
SBI-FMO	Repayment or conversion after 66 months	6-month T-bill rate + 450 basis points Payable per annum	705,239,278	706,706,095
DGGF	Repayment or conversion after 60 months	6-month T-bill rate+700 basis points Payable per annum	1,768,988,516	–
BIO	Repayment or conversion after 60 months	6-month LIBOR + 550 basis points Payable per annum	1,453,890,011	–
Less: Initial transaction cost			(33,676,905)	(15,374,541)
Total			4,210,565,525	1,008,027,823

28 Retirement benefit obligation

28.1 Defined benefit liability*

	2019 LKR	2018 LKR
Defined benefit liability (Note 28.1.1)	479,575,300	354,854,450
Total	479,575,300	354,854,450

** Defined benefit liability classified under other liability in 31 December 2018 has been reclassified and separately recorded as retirement benefit obligation and comparative figure in this financial statement is amended. (Refer Note 44)*

28.1.1 Movement in defined benefit obligation

	2019 LKR	2018 LKR
Opening balance as at 1 January	354,854,450	257,476,102
Net benefit expense (Note 28.1.2)	133,715,592	100,585,945
Benefit paid	(8,994,741)	(3,207,597)
Closing balance as at 31 December	479,575,300	354,854,450

28.1.2 Net benefit expense

	2019 LKR	2018 LKR
Interest cost	43,647,097	28,359,486
Current service cost	48,480,714	26,231,153
	92,127,811	54,590,639
Amounts recognised in the other comprehensive income		
Actuarial gain/(loss) on obligations	41,587,781	45,995,306
Total expense for the year	133,715,592	100,585,945

28.1.3 The principal financial assumptions used are as follows:

Messrs. Piyal S Goonetilleke actuaries, carried out an actuarial valuation of the defined benefit plan gratuity on 31 December 2019. Appropriate and compatible assumptions were used in determining the cost of retirement benefits. The principal assumptions used are as follows:

	2019	2018
Long term interest rate (%)	10.25	12.30
Future salary increase rate (%)	7.75	11.30
Retirement age (years)	55	55

Mortality – GA 1983 Mortality Table issued by the Institute of Actuaries London. The average duration of the defined benefit plan obligation at the end of the reporting period is 10 years.

28.2 Sensitivity analysis on discounting rate and salary increment rate to Statement of Financial Position and Comprehensive Income

		2019		2018	
Assumption	Rate change	Impact to financial position-increment/(reduction) of liability	Impact to Comprehensive Income-Charged/(reversal)	Impact to financial position increment/(reduction) of liability	Impact to comprehensive income-charged/(reversal)
Discount rate	1+	(35,226,669)	(35,226,669)	(31,422,769)	(31,422,769)
Discount rate	1–	40,392,239	40,392,239	36,365,685	36,365,685
Salary increment rate	1+	39,697,560	39,697,560	35,249,002	35,249,002
Salary increment rate	1–	(35,236,014)	(35,236,014)	(31,042,941)	(31,042,941)

28.3 The expected benefit payout in the future years of retirement gratuity

	2019 LKR	2018 LKR
Within next 12 months	44,481,682	29,520,864
Between 2 and 5 years	342,084,695	209,523,632
Beyond 5 years	350,405,795	471,331,175

29 *Other liability**

	2019 LKR	2018 LKR
Special purpose project funds	405,698,608	407,765,490
Lease liability (Note 29.1)	591,658,015	–
Accruals and other payables	494,402,117	360,067,912
Total	1,491,758,740	767,833,402

** Defined benefit liability classified under other liability in 31 December 2018 has been reclassified and separately recorded as retirement benefit obligation and comparative figure in this Financial Statement is amended. (Refer Note 44)*

29.1 Movement in lease liabilities

	2019 LKR	2018 LKR
Opening balance as at 1 January	–	–
Effect of adoption of SLFRS 16 as at 1 January	472,702,962	–
Additions	239,253,218	–
Accretion of interest	43,244,491	–
Payments during the year	(163,542,656)	–
Closing balance as at 31 December	591,658,015	–

29.2 Maturity analysis of lease liabilities

	2019 LKR	2018 LKR
Less than 1 year	9,731,499	–
Between 1 and 5 years	345,051,391	–
More than 5 years	236,875,125	–
Total lease liabilities as at 31 December	**591,658,015**	–

30 Stated capital

	2019 LKR	2018 LKR
Ordinary shares – Issued and fully paid	5,921,538,126	5,921,538,126
Total	**5,921,538,126**	5,921,538,126

30.1 Details of ordinary shares issued and fully paid

	Opening balance as at 1 January 2019 Number	Issued for script during the year Number	Redemptions/ Transfers Number	Closing balance as at 31 December 2019 Number
Ordinary shares – Voting	56,308,252	–	–	56,308,252
	56,308,252	–	–	56,308,252

	Opening balance as at 1 January 2019 LKR	Issued for cash during the year LKR	Redemptions/ Transfers LKR	Closing balance as at 31 December 2019 LKR
Ordinary shares value – Voting	5,921,538,126	–	–	5,921,538,126
	5,921,538,126	–	–	5,921,538,126

31 Statutory reserve fund

	2019 LKR	2018 LKR
Opening balance as at 1 January	215,611,469	197,763,963
Transfer during the period	12,670,255	17,847,506
Closing balance as at 31 December	**228,281,724**	215,611,469

32 Retained earnings

	2019 LKR	2018 LKR
Opening balance as at 1 January	1,280,762,267	1,340,503,862
Impact of adoption of SLFRS 9 as at 1 January	–	(37,054,387)
Profit for the year	223,461,894	323,833,499
Transfers to other reserves	(12,670,255)	(17,847,506)
Scrip dividend	–	(191,726,035)
Cash dividend	–	(136,947,168)
Closing balance as at 31 December	**1,491,553,906**	1,280,762,267
Dividend per share	–	5.8

33 Other reserves

2019	Opening balance as at 1 January 2019 LKR	Movement/ transfers LKR	Closing balance as at 31 December 2019 LKR
General reserve	46,656,973	–	46,656,973
Available for sale/fair value through OCI reserve	(15,842,090)	(3,209,534)	(19,051,624)
Total	**30,814,883**	**(3,209,534)**	**27,605,349**

2018	Opening balance as at 1 January 2018 LKR	Movement/ transfers LKR	Closing balance as at 31 December 2018 LKR
General reserve	46,656,973	–	46,656,973
Available-for-sale/fair value through OCI reserve	(12,453,979)	(3,388,111)	(15,842,090)
Total	34,202,994	(3,388,111)	30,814,883

34 Contingent liabilities and commitments

34.1 Bank guarantees

	2019 LKR	2018 LKR
Bank guarantees	177,752,357	182,986,032
Total	**177,752,357**	182,986,032

34.2 Litigation Against the Bank

Litigation is a common occurrence in the banking industry due to the nature of the business undertaken. The Bank has formal controls and policies for managing legal claims. Once professional advice has been obtained and the amount of loss reasonably estimated, the Bank makes adjustments to account for any adverse effects which the claims may have on its financial standing. At the year end, the Bank had several unresolved legal claims.

Following cases are filed against the Bank:

Legal status	Case numbers
1. Cases filed against the Bank with respect to mortgaged property and title of property	
– District courts	L 17/11, DMR 496/15,
	M/10238, MB/1935
	6940/P, 218/L , 7628/T
2. Cases filed against the Bank to restraining the payment of Bank Guarantee Bonds	
– District Court	SPL 252/11, 2440/M
3. Appeals filed by the customers against the court orders delivered in favour of the Bank	
– District Court	DMB 5/2016
– High Court Civil Appeal	WP/HCCA/ COL/272/15(F) HCCA/82/2017 (F)
4. Cases filed by customers to obtain injunction orders to restaining the auction of property mortgaged	
– Commercial High Court	CHC/629/19/MR
– Supreme Court	SC/HC/LA/83/2019
5. Cases filed against the Bank over the repossession of vehicles	
– District Court	DSP 178/09

For the year ended 31 December

Legal status	Case numbers
6. Cases filed against the Bank over the loan facilities to claiming right for the ceased assets by the guarantors	
– District Court	207/CL, 31/18 CL, 17615/M/17
	17613/M/17, 13/17/CL, 53/CL
	551/CL, 552/CL, 553/CL
7. Cases filed against the Bank by the employees and former Directors	
– District Court	DMR/4015/17, 6495/SPL
– Labour Tribunal	LT/BT/344/2017

Other than those disclosed above there is no case filed against the Bank which would have material impact on the financial position of the Bank.

35 Events occurring after the reporting date

There are no material events after the reporting date that require adjustments to or disclosure in the Financial Statements.

36 Related party disclosure

The Bank carries out transaction in the ordinary course of business with the parties who are defined as related parties in the Sri Lanka Accounting Standard – LKAS 24 ("Related Party Disclosures"), the details of which are reported below:

36.1 Transactions with other related parties

According to the LKAS 24, FMO consider as a related party (Significant investor) and all transaction with FMO are given below.

	2019 LKR	2018 LKR
Interest and capital repayment	526,112,499	240,127,258
Reimbursement of expenses	889,181	2,465,459

36.2 Transactions with key management personnel (KMP)

Key Management Personnel include: the Chairman, the Board of Directors, and Chief Executive Officer, Deputy Chief Executive Officer of the Bank. Transactions with close family members of Key Management Personnel are also taken into account in the transactions with Key Management Personnel. The Same term, including interest/commission rates & security, as for comparable transaction with person of a similar standing or, where applicable, with the employees. The transaction did not involve more than the normal risk of repayment or present other unfavourable features.

36.2.1 Key management personnel compensation

	2019 LKR	2018 LKR
Short-term employee benefits	50,627,995	33,113,000
Post employment benefits	2,100,000	2,080,800

36.2.2 Other transactions (loans and receivables) with key management personnel – Balance outstanding

	2019 LKR	2018 LKR
Opening balance as at 1 January	2,029,183	2,352,976
Granting	–	–
Repayments	(427,240)	(323,793)
Closing balance as at 31 December	1,601,943	2,029,183
Interest income	253,941	300,885

36.2.3 Deposits and investment from key management personnel – Balance outstanding

	2019 LKR	2018 LKR
Deposits accepted and reviewed during the period	39,587,156	2,982,512
Balance as at 31 December	16,630,438	163,274
Interest expenses	349,401	10,138

36.2.4 Other payment to key management personnel

	2019 LKR	2018 LKR
Cash dividend	–	157,494

36.2.5 Shareholdings by key management personnel

	2019 Number	2018 Number
Number of shares held by KMP	199,450	75,243

36.2.6 Term and conditions of transaction with related parties

All related party transaction are carried out in the normal course of business and transacted at normal business terms. Transaction from related parties are made on terms equivalent to those that prevail in arm's length transaction and comparable with those that would have been charged from unrelated companies. All related party outstanding balances at the year-end are secured and are to be settled in cash.

37 Assets pledged

Bank has pledged from the lease portfolios sum of LKR 1,222,145,124/- (2018 – LKR 1,892,536,929/-) for the Securitised Borrowings.

38 Analysis of financial instruments by measurement basis

As at 31 December 2019	Amortised cost LKR	FVTPL LKR	FVTOCI LKR	Total LKR
Financial assets				
Cash and cash equivalents	2,429,790,570	–	–	2,429,790,570
Placements with banks	5,628,094,545	–	–	5,628,094,545
Financial assets at fair value through profit or loss	–	3,527,310,141	–	3,527,310,141
Financial assets at amortised cost				
– Loans and receivables to other customers	85,823,334,862	–	–	85,823,334,862
– Debt and other instruments	6,998,924,881	–	–	6,998,924,881
Financial assets measured at fair value through other comprehensive income	–	–	56,938,514	56,938,514
Total financial assets	100,880,144,858	3,527,310,141	56,938,514	104,464,393,514
Financial liabilities				
Due to other customers	72,431,923,465	–	–	72,431,923,465
Other borrowings	20,299,717,968	–	–	20,299,717,968
Debt Securities issued	1,014,034,248	–	–	1,014,034,248
Subordinated term debts	4,210,565,525	–	–	4,210,565,525
Total financial liabilities	97,956,241,206	–	–	97,956,241,206

As at 31 December 2018	Amortised cost LKR	FVTPL LKR	FVTOCI LKR	Total LKR
Financial assets				
Cash and cash equivalents	4,171,938,630	–	–	4,171,938,630
Placements with banks	9,528,425,565	–	–	9,528,425,565
Financial assets at fair value through profit or loss		146,103,330	–	146,103,330
Financial assets at amortised cost				
– Loans and receivables to other customers	77,507,021,162	–	–	77,507,021,162
– Debt and other instruments	3,405,600,286	–	–	3,405,600,286
Financial assets measured at fair value through other comprehensive income	–	–	60,148,048	60,148,048
Total financial assets	94,612,985,642	146,103,330	60,148,048	94,819,237,021
Financial liabilities				
Due to other customers	67,474,821,535	–	–	67,474,821,535
Other borrowings	15,420,967,962	–	–	15,420,967,962
Debt Securities issued	4,198,547,716	–	–	4,198,547,716
Subordinated term debts	1,008,027,823	–	–	1,008,027,823
Total financial liabilities	88,102,365,036	–	–	88,102,365,036

39 Fair value of financial instruments

39.1 Financial instruments recorded at fair value

The following is a description of how fair values are determined for financial instrument that are recorded at fair value using valuation techniques. These incorporate the Bank's estimate of assumption that a market participant would make when valuing the instrument.

Fair value through other comprehensive income

Fair value through OCI valued using valuation techniques or pricing models primary consist of unquoted.

Fair value through profit and loss

Quoted equities, Sri Lanka Government securities – Treasury bonds and unit trust included in financial assets fair value through profit or loss are valued using market price.

39.2 Determination of fair value and fair value hierarchy

The Bank uses the following hierarchy for determining and disclosing the fair value of financial instruments by valuation technique.

Level 1 : Quoted (unadjusted) prices in active markets for identical assets or liabilities.

Level 2 : Other techniques for which all inputs which have a significant effect on the recorded fair value are observable, either directly or indirectly.

Level 3 : Techniques which use inputs that have a significant effect on the recorded fair value that are not based on observable market data.

39.2.1 Analysis of financial instruments recorded at fair value by level of fair value hierarchy

	As at 31 December 2019			
	Level 1 LKR	Level 2 LKR	Level 3 LKR	Total LKR
Financial assets fair value through profit or loss				
Sri Lanka Government securities – Treasury bills	–	46,519,350	–	46,519,350
Unit trusts	–	3,480,790,791	–	3,480,790,791
Fair value through other comprehensive income				
Unquoted equity securities	–	–	56,938,514	56,938,514
Total	–	3,527,310,141	56,938,514	3,584,248,655

	As at 31 December 2018			
	Level 1 LKR	Level 2 LKR	Level 3 LKR	Total LKR
Financial assets fair value through profit or loss				
Sri Lanka Government securities – Treasury bonds	–	–	–	–
Unit trusts	–	146,103,330	–	146,103,330
Fair value through other comprehensive income				
Unquoted equity securities	–	–	60,148,048	60,148,048
Total	–	146,103,330	60,148,048	206,251,378

The following table shows the total gains/(losses) recognised in profit or loss during the year relating to assets and liabilities held at the year end.

	2019 LKR	2018 LKR
Net gain/(loss) from trading	1,264,727	–
Net fair value gain/(loss) of financial assets at fair value through profit or loss		
Sri Lanka Government securities – Treasury bonds	(58,050)	(942,414)
Unit trusts	114,947,499	281,114,474
Total gain/(loss)	116,154,176	280,172,060

39.3 Fair value of financial assets and liabilities not carried at fair value

Set out below is a comparison, by class, of the carrying amounts and fair values of the Bank's Financial Instruments that are not carried at fair value in the Financial Statements. This table does not include the fair values of non-financial assets and non–financial liabilities.

	Level	As at 31 December 2019	
		Carrying Value LKR	Fair Value LKR
Financial assets			
Cash and cash equivalents	Note*	2,429,790,570	2,429,790,570
Placements with banks	Note*	5,628,094,545	5,628,094,545
Financial assets at amortised cost			
– Loans and receivables to other customers	2	85,823,334,862	92,356,556,375
– Debt and other instruments	Note*	6,998,924,881	6,998,924,881
Total financial assets		100,880,144,858	107,413,366,371
Financial liabilities			
Due to other customers	2	72,431,923,465	66,969,704,982
Other borrowings	2	20,299,717,968	21,651,988,374
Debt securities issued	2	1,014,034,248	1,014,034,248
Subordinated term debts	2	4,210,565,525	4,210,565,525
Total financial liabilities		97,956,241,206	93,846,293,129

	Level	As at 31 December 2018	
		Carrying value LKR	Fair value LKR
Financial assets			
Cash and cash equivalents	Note*	4,171,938,630	4,171,938,630
Placements with banks	Note*	9,528,425,565	9,528,425,565
Financial assets at amortised cost			
– Loans and receivables to other customers	2	77,507,021,162	77,781,165,229
– Debt and other instruments	Note*	3,405,600,286	3,405,600,286
Total financial assets		94,612,985,643	94,887,129,710
Financial liabilities			
Due to other customers	2	67,474,821,535	57,889,168,348
Other borrowings	2	15,420,967,962	15,418,148,997
Debt securities issued	2	4,198,547,716	4,198,547,716
Subordinated term debts	2	1,008,027,823	1,008,027,823
Total financial liabilities		88,102,365,036	78,513,892,884

Note*

Fair value of financial assets and liabilities not carried at fair value

The following describes the methodologies and assumptions used to determine fair values for those financial instruments which are not already recorded at fair value in the Financial Statements:

Assets for which fair value approximates carrying value

For financial assets and financial liabilities that have a short term maturity (less than a year) it is assumed that the carrying amounts approximate their fair value. This assumption is also applied to demand deposits and savings accounts without a specific maturity. Loans and advances to customers with a variable rate are also considered to be carried at fair value.

Fixed rate financial instruments

The fair value of fixed rate financial assets and liabilities carried at amortised cost are estimated by comparing market interest rates when they were first recognised with current market rates for similar financial instruments. The estimated fair value of fixed interest bearing deposits is based on discounted cash flows using prevailing interest rates of the Bank.

40 *Segment reporting*

	As at 31 December 2019				
	Banking LKR	Leasing LKR	Treasury LKR	Pawning LKR	Total LKR
Interest income	12,509,868,962	1,090,964,365	1,239,351,727	239,138,751	15,079,323,806
Interest expenses	(6,977,189,168)	(573,254,531)	(1,674,257,285)	(157,827,936)	(9,382,528,920)
Net interest income	5,532,679,794	517,709,835	(434,905,558)	81,310,816	5,696,794,886
Fee and commission income	201,937,822	35,718,639	–	–	237,656,461
Fee and commission expenses	(6,012,622)	(494,004)	–	–	(6,506,626)
Net fee and commission income	195,925,201	35,224,634	–	–	231,149,835
Net gains/(losses) from trading	–	–	1,264,727	–	1,264,727
Net fair value gains/(losses) of financial assets at fair value through profit or loss	–	–	114,889,449	–	114,889,449
Net other operating income	90,727,985	–	240,800	–	90,968,785
Total operating income	5,819,332,979	552,934,468	(318,510,583)	81,310,815	6,135,067,682
Impairment for loans and other losses	(809,523,806)	(112,639,820)	4,594,178	135,942	(917,433,506)
Net operating income	5,009,809,173	440,294,648	(313,916,405)	81,446,757	5,217,634,176
Depreciation and amortisation expenses	(390,191,470)	(32,058,616)	(116,161)	(8,826,350)	(431,192,597)
Segment result	4,619,617,703	408,236,032	(314,032,566)	72,620,406	4,786,441,579
Un-allocated expenses					(3,536,420,975)
Value Added Tax (VAT) on financial services					(386,522,109)
Nation Building Tax (NBT) on financial services					(51,106,360)
Debt repayment Levy					(226,564,695)
Profit before tax					585,827,440
Tax expenses					(332,422,344)
Profit for the year					253,405,096
Other comprehensive income					
Other comprehensive income for the year net of tax					(33,152,736)
Total comprehensive income for the year					220,252,360
Segment assets	77,683,515,936	6,382,574,185	18,641,058,651	1,757,244,741	104,464,393,513
Un-allocated assets	–	–	–	–	3,319,230,816
Total assets	77,683,515,936	6,382,574,185	18,641,058,651	1,757,244,741	107,783,624,329
Segment liabilities	74,448,885,176	6,116,812,903	17,864,871,567	1,684,075,578	100,114,645,224
Total equity	–	–	–	–	7,668,979,105
Total liabilities	74,448,885,176	6,116,812,903	17,864,871,567	1,684,075,578	107,783,624,329
Addition to non-current assets	448,506,665	36,849,865	–	10,145,473	495,502,003

	As at 31 December 2018				
	Banking LKR	Leasing LKR	Treasury LKR	Pawning LKR	Total LKR
Interest income*	10,977,258,277	827,449,414	1,161,471,770	180,607,695	13,146,787,156
Interest expenses	(6,611,642,530)	(474,369,619)	(1,221,112,089)	(116,633,491)	(8,423,757,729)
Net interest income	4,365,615,747	353,079,794	(59,640,319)	63,974,204	4,723,029,427
Fee and commission income*	164,143,138	32,618,933	–	–	196,762,071
Fee and commission expenses	(4,102,534)	(294,347)	–	–	(4,396,881)
Net fee and commission income	160,040,604	32,324,586	–	–	192,365,190
Net fair value gain/(loss) of financial assets at fair value through profit or loss	–	–	280,172,060	–	280,172,060
Net other operating income	20,334,514	–	476,587	–	20,811,101
Total operating income	4,545,990,865	385,404,381	221,008,326	63,974,204	5,216,377,778
Impairment for loans and other losses	(470,940,030)	(51,990,820)	(6,127,309)	3,214,279	(525,843,880)
Net operating income	4,075,050,835	333,413,561	214,881,017	67,188,484	4,690,533,898
Depreciation and amortisation expenses	(205,765,548)	(14,763,188)	(101,863)	(3,629,832)	(224,260,432)
Segment result	3,869,285,287	318,650,373	214,779,154	63,558,651	4,466,273,466
Un-allocated expenses					(3,353,205,201)
Value Added Tax (VAT) on financial services					(362,940,818)
Nation Building Tax (NBT) on financial services					(52,702,722)
Debt repayment levy					(53,282,253)
Profit before tax					644,142,473
Tax expenses					(287,192,354)
Profit for the year					356,950,119
Other comprehensive income					
Other comprehensive income for the year net of tax					(36,504,731)
Total comprehensive income for the year					320,445,388
Segment assets	71,147,289,913	5,104,648,758	13,140,277,228	1,255,082,491	90,647,298,390
Un-allocated assets	–	–	–	–	6,170,468,795
Total assets	71,147,289,913	5,104,648,758	13,140,277,228	1,255,082,491	96,817,767,185
Segment liabilities	70,144,010,272	5,032,665,831	12,954,980,323	1,237,384,014	89,369,040,440
Total equity	–	–	–	–	7,448,726,745
Total liabilities	70,144,010,272	5,032,665,831	12,954,980,323	1,237,384,014	96,817,767,185
Addition to non-current assets	199,134,282	14,287,411	–	3,512,853	216,934,546

** Late fee charged from overdue rentals classified under net fee and commission income in 31 December 2018 has been reclassified to interest income and comparative figure in this Financial Statement is amended. (Refer Note 44)*

41 *Maturity analysis of assets and liabilities*

The following table shows an analysis of assets and liabilities according to when they are expected to be recovered or settled:

	As at 31 December 2019			As at 31 December 2018		
	Within 12 months LKR	After 12 months LKR	Total LKR	Within 12 months LKR	After 12 months LKR	Total LKR
Assets						
Cash and cash equivalents	2,429,790,570	–	2,429,790,570	4,171,938,629	–	4,171,938,629
Placements with banks	4,177,742,545	1,450,352,000	5,628,094,545	9,528,425,565	–	9,528,425,565
Financial assets fair value through profit or loss	3,527,310,141	–	3,527,310,141	146,103,330	–	146,103,330
Financial assets at amortised cost						
– Loans and receivables to other customers	18,200,097,573	67,623,237,289	85,823,334,862	17,213,381,317	60,293,639,845	77,507,021,162
– Debt and other instruments	6,948,924,881	50,000,000	6,998,924,881	3,316,920,287	88,680,000	3,405,600,287
Financial assets measured at fair value through other comprehensive income	–	56,938,514	56,938,514	–	60,148,048	60,148,048
Property, plant and equipment	–	645,231,444	645,231,444	–	704,738,491	704,738,491
Right of use assets	11,907,855	639,362,893	651,270,748	–	–	–
Investment properties	–	21,278,600	21,278,600	–	22,334,630	22,334,630
Intangible assets	–	308,444,541	308,444,541	–	3,727,725	3,727,725
Deferred tax assets	–	232,481,661	232,481,661	–	69,414,926	69,414,926
Other assets	1,460,523,822	–	1,460,523,822	1,198,314,392	–	1,198,314,392
Total assets	36,756,297,388	71,027,326,942	107,783,624,329	35,575,083,520	61,242,683,665	96,817,767,185
Liabilities						
Due to other customers	51,618,024,041	20,813,899,425	72,431,923,466	47,596,788,688	19,878,032,846	67,474,821,534
Other borrowings	8,444,199,647	11,855,518,321	20,299,717,968	6,221,139,240	9,199,828,723	15,420,967,963
Debt securities issued	1,014,034,248	–	1,014,034,248	3,233,987,716	964,560,000	4,198,547,716
Subordinated term debts	10,243,764	4,200,321,761	4,210,565,525	15,058,060	992,969,761	1,008,027,823
Retirement benefit obligation*	–	479,575,300	479,575,300	–	354,854,450	354,854,450
Current tax liabilities	187,069,978	–	187,069,978	143,987,553	–	143,987,552
Other liabilities*	909,832,224	581,926,516	1,491,758,740	767,833,402	–	767,833,402
Total liabilities	62,183,403,902	37,349,314,806	100,114,645,225	57,978,794,659	31,390,245,780	89,369,040,440
Net asset/(liability)	(25,427,106,514)	33,678,012,136	7,668,979,105	(22,403,711,138)	29,852,437,885	7,448,726,745

** Defined benefit liability classified under other liability in 31 December 2018 has been reclassified and separately recorded as retirement benefit obligation and comparative figure in this Financial Statement is amended. (Refer Note 44)*

42 *Risk management*

42.1 Introduction

Risk is inherent in the Bank's activities but is managed through a process of ongoing identification, measurement and monitoring, subject to risk limits and other controls. This process of risk management is critical to the Bank's continuing profitability and each individual within the Bank is accountable for the risk exposures relating to his or her responsibilities. The Bank is exposed to credit risk, liquidity risk and market risk and operational risk.

The independent risk control process does include business risks such as changes in the environment, technology and industry. The Bank's policy is to monitor those business risks through the bank's strategic planning process.

Risk management structure

The Board of Directors is responsible for the overall risk management approach and for approving the risk management strategies and principles.

The Board has appointed the Board subcommittee which has the responsibility to monitor the overall risk process within the Bank.

The Risk Committee has the overall responsibility for the development of the risk strategy and implementing principles, frameworks, policies and limits. The Risk Committee is responsible for managing risk decisions and monitoring risk levels and reports on a quarterly basis.

The Risk Management Unit is responsible for implementing and maintaining risk related procedures to ensure an independent control process is maintained. The unit works closely with the Risk Committee to ensure that procedures are compliant with the overall framework.

The Risk management Unit is responsible for monitoring compliance with risk principles, policies and limits across the Bank. This unit responsible for the independent control of risks, including monitoring the risk of exposures against limits and the assessment of risks of new products and structured transactions. This unit also ensures the complete capture of the risks in risk measurement and reporting systems. Exceptions are reported on a periodically, where necessary, to the Risk Committee and the relevant actions are taken to address exceptions and any areas of weakness.

Bank Treasury is responsible for managing the Bank's assets and liabilities and the overall financial structure.

It is also primarily responsible for the funding and liquidity risks of the Bank.

The Bank's policy is that risk management processes throughout the Bank are audited annually by the Internal Audit function, which examines both the adequacy of the procedures and the Bank's compliance with the procedures. Internal Audit discusses the results of all assessments with management and reports its findings and recommendations to the Audit Committee.

Risk measurement and reporting systems

Monitoring and controlling risks is primarily performed based on limits established by the Bank. These limits reflect the business strategy and market environment of the Bank as well as the level of risk that the bank is willing to accept, with additional emphasis on selected industries. In addition, the bank's policy is to measure and monitor the overall risk bearing capacity in relation to the aggregate risk exposure across all risk types and activities.

Information compiled from all the businesses is examined and processed in order to analyse, control and identify risks on a timely basis. This information is presented and explained to the Board of Directors, the Risk Committee and the head of each business division. The report includes aggregate credit exposure, liquidity ratios and risk profile changes. On a monthly basis, detailed reporting of industry, customer and geographic risks takes place. Senior management assesses the appropriateness of the allowance for credit losses on a monthly basis. The Board subcommittee receives a comprehensive risk report once a quarter which is designed to provide all the necessary information to assess and conclude on the risks of the Bank.

For all levels throughout the Bank, specifically tailored risk reports are prepared and distributed in order to ensure that all business divisions have access to extensive, necessary and up-to-date information. A daily briefing is given to the CEO and all other relevant members of the bank on the utilisation of market limits, proprietary investments, liquidity and any other risk developments.

Risk mitigation

As part of its overall risk management, the Bank uses several strategies and other instruments to manage exposures resulting from changes in interest rates, foreign currencies, equity risks, credit risks and exposures arising from forecast transactions. In accordance with the Bank's policy, the risk profile of the Bank is assessed by the appropriate level of seniority within the Bank. The Bank actively uses collateral to reduce its credit risks.

Excessive risk concentration

Concentrations arise when a number of counterparties are engaged in similar business activities, or activities in the same geographical region, or have similar economic features that would cause their ability to meet contractual obligations to be similarly affected by changes in economic, political or other conditions. Concentrations indicate the relative sensitivity of the bank's performance to developments affecting a particular industry or geographical location.

In order to avoid excessive concentrations of risk, the bank's policies and procedures include specific guidelines to focus on maintaining a diversified portfolio. Identified concentrations of credit risks are controlled and managed accordingly.

42.2 *Credit risk*

Credit risk is the risk that the Bank will incur a loss because its customers or counterparties fail to discharge their contractual obligations. The Bank manages and controls credit risk by setting limits on the amount of risk it is willing to accept for individual counterparties and for geographical and industry concentrations, and by monitoring exposures in relation to such limits.

The Bank has established a credit quality review process to provide early identification of possible changes in the creditworthiness of counterparties, including regular collateral revisions. Counterparty limits are established by the use of a credit risk evaluation system, which assigns each counterparty a risk. The credit quality review process aims to allow the Bank to assess the potential losses a result of the risks to which it is exposed and take corrective action.

Credit-related commitments risks

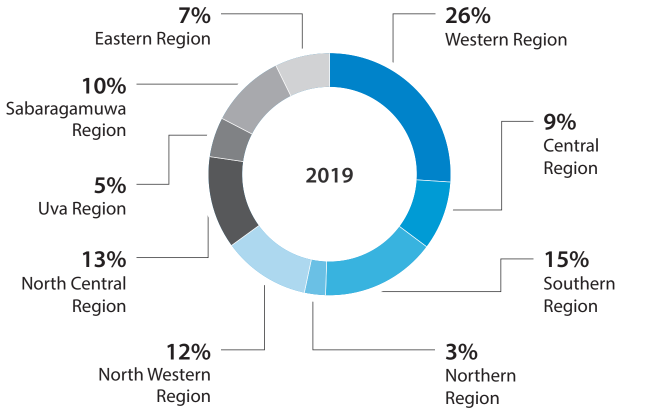
The Bank makes available to its customers guarantees which may require that the Bank makes payments on their behalf and enters into commitments to extend credit lines to secure their liquidity needs. Such commitments expose the Bank to similar risks to loans and are mitigated by the same control processes and policies.

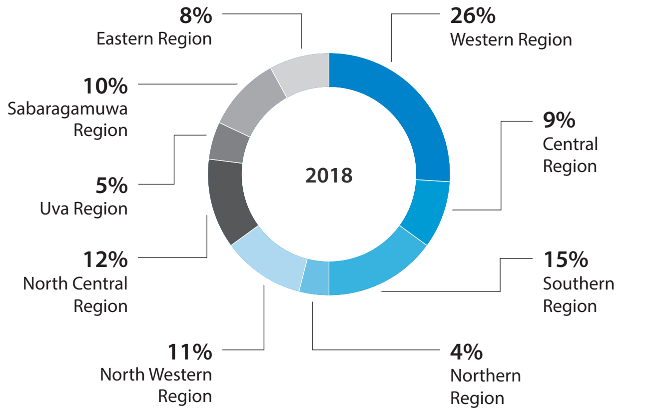
Risk concentrations: maximum exposure to credit risk without taking account of any collateral and other credit enhancements.

The Bank's concentrations of risk are managed by client/counterparty, by geographical region and by industry sector. The maximum credit exposure to any client or counterparty as of 31 December 2019 was LKR 313 Mn.

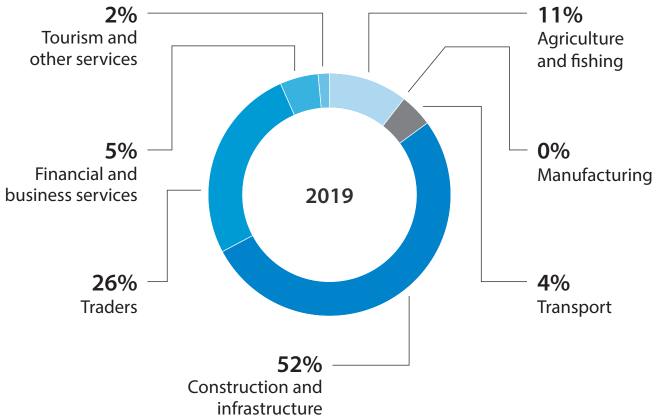
The following table shows the maximum exposure to credit risk for the components of the Statement of Financial Position, by geography of counterparty and by industry before the effect of mitigation through the use of master netting and collateral agreements. Where financial instruments are recorded at fair value, the amounts shown represent the current credit risk exposure but not the maximum risk exposure that could arise in the future as a result of changes in values.

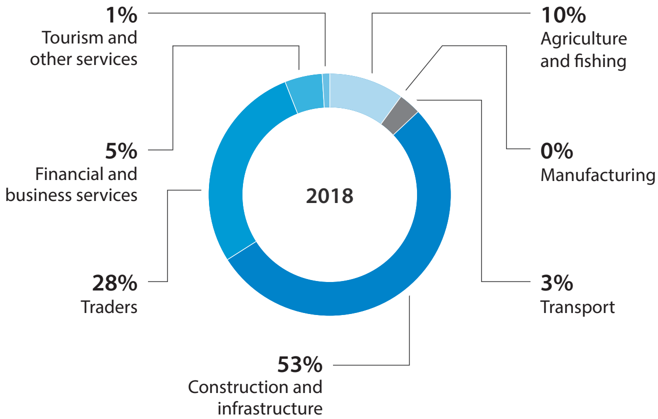
Geographical analysis





Industry analysis





Collateral and other credit enhancements

The amount and type of collateral required depends on an assessment of the credit risk of the counterparty.

Guidelines are implemented regarding the acceptability of types of collateral and valuation parameters.

The main types of collateral obtained are as follows:

- Cash or securities
- Real estate properties
- Mortgages over residential properties
- Movable assets – Motor vehicle
- Gold

The Bank also obtains guarantees from parent companies for loans to their subsidiaries.

Management monitors the market value of collateral, requests additional collateral in accordance with the underlying agreement and monitors the market value of collateral obtained during its review of the adequacy of the allowance for impairment losses.

It is the Bank's policy to dispose of repossessed properties in an orderly fashion. The proceeds are used to reduce or repay the outstanding claim. In general, the Bank does not occupy repossessed properties for business use.

42.2.1 Maximum exposure credit risk by class of financial assets

	As at 31 December 2019		As at 31 December 2018	
	Maximum exposure to credit risk LKR	Net exposure LKR	Maximum exposure to credit risk LKR	Net exposure LKR
Cash and cash equivalents	2,429,790,570	2,429,790,570	4,171,938,630	4,171,938,630
Placements with banks	5,628,094,545	5,628,094,545	9,528,425,565	9,528,425,565
Financial assets fair value through profit or loss	3,527,310,141	3,527,310,141	146,103,330	146,103,330
Financial assets at amortised cost				
– Loans and receivables to other customers	88,720,800,911	74,451,537,819	79,482,459,527	65,213,196,435
– Debt and other instruments	6,998,924,881	2,666,271,222	3,405,600,286	471,378,656
Total	107,304,921,048	88,703,004,297	96,734,527,338	79,531,042,616

Credit quality by class of financial assets

	As at 31 December 2019			
	Neither past due nor impaired LKR	Past due but not impaired LKR	Individually impaired LKR	Total LKR
Cash and cash equivalents	2,429,790,570	–	–	2,429,790,570
Placements with banks	5,628,094,545	–	–	5,628,094,545
Financial assets fair value through profit or loss	3,527,310,141	–	–	3,527,310,141
Financial assets at amortised cost				
– Loans and receivables to other customers	71,008,197,804	14,935,693,040	2,776,910,068	88,720,800,912
– Debt and other instruments	3,405,600,287	–	–	3,405,600,287
Total	85,998,993,348	14,935,693,040	2,776,910,068	103,711,596,455

	As at 31 December 2018			
	Neither past due nor impaired LKR	Past due but not impaired LKR	Individually impaired LKR	Total LKR
Cash and cash equivalents	4,171,938,630	–	–	4,171,938,630
Placements with banks	9,528,425,565	–	–	9,528,425,565
Financial assets fair value through profit or loss	146,103,330	–	–	146,103,330
Financial assets at amortised cost				–
– Loans and receivables to other customers	64,662,927,979	13,673,100,463	1,146,431,087	79,482,459,528
– Debt and other instruments	3,405,600,287	–	–	3,405,600,287
Total	81,914,995,791	13,673,100,463	1,146,431,087	96,734,527,340

	As at 31 December 2019 Past due but not impaired				
	Less than 30 days LKR	**31 to 60 days LKR**	**61 to 90 days LKR**	**More than 90 days LKR**	**Total LKR**
Loans and receivables to other customers (without impairment)	**7,201,475,238**	**3,784,482,626**	**538,536,434**	**3,411,198,742**	**14,935,693,040**

	As at 31 December 2018 Past due but not impaired				
	Less than 30 days LKR	31 to 60 days LKR	61 to 90 days LKR	More than 90 days LKR	Total LKR
Loans and receivables to other customers (without impairment)	6,081,797,677	4,413,998,529	222,108,245	2,955,196,012	13,673,100,463

Impairment assessment

definition of default and cure

The Bank considers a financial instrument defaulted and therefore Stage 3 (credit-impaired) for ECL calculations in all cases when the borrower becomes 90 days past or three instalments in arrears due on its contractual payments. The Bank considers treasury and interbank balances defaulted and takes immediate action when the required intraday payments are not settled by the close of business as outlined in the individual agreements. As a part of a qualitative assessment of whether a customer is in default, the Bank also considers a variety of instances that may indicate unlikeliness to pay. When such events occur, the Bank carefully considers whether the event should result in treating the customer as defaulted and therefore assessed as Stage 3 for ECL calculations or whether Stage 2 is appropriate. Such events (among others) include;

- When contractual payments of a customer are more than 30 days past due;
- When reasonable and supportable forecasts of future economic conditions directly affect the performance of a customer/group of customers, portfolios or instruments;
- When the value of collateral is significantly reduced and/or realisability of collateral is doubtful. Limits shall be set and documented by licensed banks;
- Modification of terms resulting in concessions, including extensions, deferment of payments, waiver of covenants etc.;
- When the customer is deceased/insolvent;
- When the Bank is unable to contact or find the customer;

It is the Bank's policy to consider a financial instrument as 'cured' and therefore re-classified out of Stage 3 when none of the default criteria have been present for at least six consecutive months. The decision whether to classify an asset as Stage 2 or Stage 1 once cured depends on the updated credit grade, at the time of the cure, and whether this indicates there has been a significant increase in credit risk compared to initial recognition.

Probability of default (PD) estimation process

Probability of Default is the estimate of the likelihood of default over a given time horizon. A default may only happen at a time horizon if the facility has not been previously derecognised and is still in the portfolio.

An early exit (EE) may occur in case of default unless the facility reverts to performing without significant modification of the contractual terms. The marginal probability of default for the period is then adjusted from the probability that an early exit occurred during the previous period.

12 Months PD

This is the estimated probability of default occurring within the next 12 months.

The 12 month PD is applied for the "Current" and "1-30 days" buckets since there is no significant deterioration in credit risk.

Lifetime PD

This is the estimated probability of default occurring over the remaining life of the financial instrument.

The lifetime PD is applied for the "31-60" days and "61-90" days buckets since there is a significant deterioration in credit risk.

The PD for the "Above 90" days category is 100% since there is objective evidence of impairment as the default has occurred.

Exposure at default (EAD)

The exposure at default represents the gross carrying amount of the financial instruments subject to the impairment calculation, addressing both the client's ability to increase its exposure while approaching default and potential early repayments too.

These components will all need to be estimated based on past experience and future expectations, for sections of the portfolio that are segmented so that they have similar credit characteristics.

Loss given default (LGD)

Loss given default is the magnitude of likely loss on exposure, and is expressed as a percentage of exposure. These LGD rates take into account the expected EAD in comparison to the amount expected to be recovered or realised from any collateral held.

The Bank segments its retail lending products into smaller homogeneous portfolios, based on key characteristics that are relevant to the estimation of future cash flows. The applied data is based on historically collected loss data and involves a wider set of transaction characteristics (e.g., product type, wider range of collateral types) as well as borrower characteristics.

For each year, closed contracts which have crossed the "Above 90" days at-least once in their lifetime are considered. LGD will factor in all cash flows subsequent to the point of default until the full settlement of the loan.

Virtually closed contracts are also be added to this data set. Virtually closed contracts are active loans which have been long outstanding. A contract is determined to be virtually closed at the point the Bank determines that the cash flows have dried up.

Significant increase in credit risk

The Bank continuously monitors all assets subject to ECLs. In order to determine whether an instrument or a portfolio of instruments is subject to 12 months ECL or life time ECL the Bank assesses whether there has been a significant increase in credit risk since initial recognition.

The Bank also applies a secondary qualitative method for triggering a significant increase in credit risk for an asset, such as moving a customer/ facility to the watch list, or the account having been restructured. In certain cases, the Bank may also consider that events as a significant increase in credit risk as opposed to a default. When estimating ECLs on a collective basis for a group of similar assets, the Bank applies the following in the categorisation of credit facilities/exposures in to stages for computation of expected credit loss.

Stage 1

- All credit facilities, which are not categorised under Stages 2 or 3 below.

Stage 2

- Credit facilities, where contractual payments of a customer are more than 30 days past due, other than the credit facilities categorised under Stage 3 below, subject to the rebuttable presumption as stated in SLFRS 9.
- All restructured loans, which are restructured up to two times (other than upgraded restructured facilities, satisfactory performing period of a minimum 90 days considered subsequent to the due date of the 1st capital and/or interest instalment post-restructure).
- Under-performing credit facilities/exposures.

Stage 3

Credit facilities where contractual payments of a customer are more than 90 days past due or 3 instalments in arrears, subject to the rebuttable presumption as stated in SLFRS 9.

- All restructured loans, which are restructured more than twice.
- All rescheduled loans, other than credit facilities/exposures (other than upgraded restructured facilities, satisfactory performing period of a minimum 90 days considered subsequent to the due date of the 1st capital and/or interest instalment post-restructure).
- All credit facilities/customers classified as non-performing as per CBSL Directions.
- Non-performing credit facilities/customers.

Grouping financial assets measured on a collective basis

As explained in Note 2.3.2 dependent on the factors below, the Bank calculates ECLs either on a collective or an individual basis.

An individual impairment assessment is performed for exposures over the Individually Significant Threshold of LKR 5 Mn. for which there is objective evidence of expected loss based on the current status of the customer, i.e. based on whether customer is performing, non-performing, rescheduled or watch-listed.

Exposures that are assessed for individual impairment and for which an impairment provision has been recognised are not included in the collective assessment of impairment. If it is determined that no objective evidence of expected loss exists for an individually assessed exposure, or assessed for objective evidence and there is no requirement for individual impairment, whether significant or not, this is included in a group of exposures with similar credit risk characteristics that are collectively assessed for impairment under the relevant bucket.

A collective assessment is performed for exposures as follows:

- Exposures that have not been individually assessed i.e. falling below the individually significant threshold
- Exposures that have been assessed for Objective Evidence of Incurred Loss and were found to have no such evidence of expected loss
- Exposures that have been individually assessed and were found not to be impaired on an individual basis based on the cash flow estimation

The bank groups these exposure in to homogeneous portfolios to extent possible so as ensure that data point available for meaningful calculations.

For accounting purposes, the bank uses an incurred loss model for the recognition of losses on impaired financial assets. This means that losses can only be recognised when objective evidence of a specific loss event has been observed. Triggering events include the following:

- Significant financial difficulty of the customer.
- A breach of contract such as a default of payment.
- Where the bank grants the customer a concession due to the customer experiencing financial difficulty.
- It becomes probable that the customer will enter bankruptcy or other financial reorganisation.
- Observable data that suggests that there is a decrease in the estimated future cash flows from the loans.

This approach differs from the expected loss model used for regulatory capital purposes in accordance with Basel III.

Individually assessed allowances

The Bank determines the allowances appropriate for each individually significant loan or advance on an individual basis, include any overdue payments of interests or infringement of the original terms of the contract. Items considered when determining allowance amounts include the sustainability of the counterparty's business plan, its ability to improve performance once a financial difficulty has arisen, projected receipts and the expected payout should bankruptcy ensue, the availability of other financial support, the realisable value of collateral and the timing of the expected cash flows. Impairment allowances are evaluated at each reporting date, unless unforeseen circumstances require more careful attention.

Collectively assessed allowances

Allowances are assessed collectively for losses on loans and advances and other debt investments that are not individually significant (including residential mortgages and unsecured consumer lending) and for individually significant loans and advances that have been assessed individually and found not to be impaired. The Bank generally bases its analyses on historical experience.

The Bank may use the aforementioned factors as appropriate to adjust the impairment allowances.

Allowances are evaluated separately at each reporting date with each portfolio.

The collective assessment is made for groups of assets with similar risk characteristics, in order to determine whether provision should be made due to incurred loss events for which there is objective evidence, but the effects of which are not yet evident in the individual loans assessments. The collective assessment takes account of data from the loan portfolio (such as historical losses on the portfolio, levels of arrears, credit utilisation, loan to collateral ratios and expected receipts and recoveries once impaired). The approximate delay between the time a loss is likely to have been incurred and the time it will be identified as requiring an individually assessed impairment allowance is also taken into consideration. Local management is responsible for deciding the length of this period which can extend for as long as one year. The impairment allowance is then reviewed by credit management to ensure alignment with the Bank's overall policy. Financial guarantees and letters of credit are assessed and provisions are made in a similar manner as for loans.

Commitments and guarantees

To meet the financial needs of customers, the Bank enters into various commitments and contingent liabilities. Even though these obligations may not be recognised on the Statement of Financial Position, they do contain credit risk and are therefore part of the overall risk of the Bank. Financial statement has separately disclosed the bank's maximum credit risk exposure for commitments and guarantees.

42.3 Liquidity risk and funding management

Liquidity risk is defined as the risk that the bank will encounter difficulty in meeting obligations associated with financial liabilities that are settled by delivering cash or another financial asset. Liquidity risk arises because of the possibility that the bank might be unable to meet its payment obligations when they fall due under both normal and stress circumstances. To limit this risk, management has arranged diversified funding sources in addition to its core deposit base, and adopted a policy of managing assets with liquidity in mind and of monitoring future cash flows and liquidity on a daily basis. The Bank has developed internal control processes and contingency plans for managing liquidity risk. This incorporates an assessment of expected cash flows and the availability of high grade collateral which could be used to secure additional funding if required.

The Bank maintains a portfolio of highly marketable and diverse assets that assumed to be easily liquidated in the event of an unforeseen interruption of cash flow. The Bank also has committed lines of credit that it can access to meet liquidity needs. In accordance with the Bank's policy the liquidity position is assessed and managed under a variety of scenarios, giving due consideration to stress factors relating to both the market in general and specifically to the Bank. The most important of these is to maintain limits on the ratio of net liquid assets to customer liabilities, to reflect market conditions. Liquid assets consist of cash, short–term bank deposits and treasury bills available for immediate sale.

The Bank stresses the importance of term accounts and savings accounts as sources of funds to finance lending to customers. They are monitored using the advances to deposit ratio, which compares loans and advances to customers as a percentage of customer savings accounts, together with term funding with a remaining term to maturity.

Analysis of financial assets and liabilities by remaining contractual maturities

The table below summarises the maturity profile of the undiscounted cash flows of the Bank's financial assets and liabilities as at 31 December. The Bank expects that many customers will not request repayment on the earliest date the Bank could be required to pay and the table does not reflect the expected cash flows indicated by the Bank's deposit retention history.

	As at 31 December 2019							
	Less than 7 Days LKR	7-30 Days LKR	1-3 Months LKR	3-12 Month LKR	1-3 Years LKR	3-5 Years LKR	Over 5 Years LKR	Total LKR
Financial assets								
Cash and cash equivalents	2,429,790,570	–	–	–	–	–	–	2,429,790,570
Investments	1,361,134,010	6,758,727,196	6,545,608,637	70,869,472	55,625,000	1,977,374,902	–	16,769,339,217
Loans and receivables to other customers	1,497,786,878	2,335,054,001	3,452,678,744	17,283,911,199	26,605,051,230	18,194,066,707	29,417,331,304	98,785,880,063
Total financial assets	5,288,711,458	9,093,781,197	9,998,287,382	17,354,780,671	26,660,676,230	20,171,441,609	29,417,331,304	117,985,009,850
Financial liabilities								
Due to other customers	2,712,403,307	4,888,405,210	12,755,524,393	32,944,756,647	13,385,221,583	5,329,197,253	4,197,664,703	76,213,173,096
Other borrowings	15,000,000	1,892,506,764	1,613,684,555	5,259,571,899	13,397,973,026	10,479,601,943	23,195,192	32,681,533,379
Debt securities issued	–	–	–	1,013,630,925	–	–	–	1,013,630,925
Total financial liabilities	2,727,403,307	6,780,911,974	14,369,208,948	39,217,959,471	26,783,194,610	15,808,799,196	4,220,859,895	109,908,337,400
Net Financial assets/ (liabilities)	2,561,308,151	2,312,869,223	(4,370,921,567)	(21,863,178,800)	(122,518,380)	4,362,642,413	25,196,471,409	8,076,672,450

	As at 31 December 2018							
	Less than 7 Days LKR	7-30 Days LKR	1-3 Months LKR	3-12 Month LKR	1-3 Years LKR	3-5 Years LKR	Over 5 Years LKR	Total LKR
Financial assets								
Cash and cash equivalents	4,171,938,630	–	–	–	–	–	–	4,171,938,630
Investments	3,466,827,144	5,764,834,724	3,834,399,122	30,599,084	96,802,800	60,148,048	–	13,253,610,920
Loans and receivables to other customers	1,416,410,358	2,117,141,125	3,269,857,395	15,520,336,642	23,958,709,739	17,900,396,885	25,835,847,050	90,018,699,193
Total financial assets	9,055,176,132	7,881,975,849	7,104,256,516	15,550,935,727	24,055,512,540	17,960,544,933	25,835,847,050	107,444,248,744
Financial liabilities								
Due to other customers	2,782,918,433	4,192,909,422	10,733,966,507	31,340,676,236	12,710,070,042	5,875,048,928	3,345,510,561	70,981,100,128
Other borrowings	–	283,182,271	1,809,763,544	4,089,634,458	9,417,061,777	5,606,886,353	45,854,456	21,252,382,859
Debt securities issued	–	–	–	1,013,630,925	–	–	–	1,013,630,925
Total financial liabilities	2,782,918,433	4,476,091,692	12,543,730,051	36,443,941,619	22,127,131,819	11,481,935,281	3,391,365,017	93,247,113,912
Net financial assets/ (liabilities)	6,272,257,699	3,405,884,156	(5,439,473,535)	(20,893,005,893)	1,928,380,720	6,478,609,652	22,444,482,033	14,197,134,832

42.4 Market risk

Market risk is the risk that the fair value or future cash flows of financial instruments will fluctuate due to changes in market variables. The Bank classifies exposures to market risk into either trading or non-trading portfolios and manages each of those portfolios separately. The market risk for the portfolio is managed and monitored using sensitivity analyses.

Interest rate risk

Interest rate risk arises from the possibility that changes in interest rates will affect future cash flows or the fair values of financial instruments.

The table below analyses the Bank's interest rate risk exposure on financial assets and liabilities.

The Bank's assets and liabilities are included at carrying amount and categorised by the earlier of contractual re-pricing or maturity dates.

Asset or liability	Interest rate sensitivity assets and liabilities as at 31 December 2019						
	Carrying amount LKR	On demand LKR	1-3 Months LKR	3-12 Months LKR	over 1 Year LKR	Non-interest LKR	Total LKR
Cash and cash equivalents	2,429,790,570	301,666,356	–	–	–	2,128,124,214	2,429,790,570
Placements with banks	5,628,094,545	1,500,000,000	2,600,000,000	77,742,545	1,450,352,000	–	5,628,094,545
Financial assets fair value through profit or loss	3,527,310,141	1,201,481,867	2,325,448,774	379,500	–	–	3,527,310,141
Loans and receivables to other customers	85,823,334,862	3,291,228,229	2,964,786,201	11,944,083,143	63,729,040,814	3,894,196,475	85,823,334,862
Debt and other instruments	6,998,924,881	2,915,851,982	3,957,838,592	75,234,306	50,000,000	–	6,998,924,884
Interest bearing assets	104,407,454,999	9,210,228,434	11,848,073,567	12,097,439,494	65,229,392,814	6,022,320,689	104,407,454,999
Due to other customers	72,431,923,465	6,904,761,138	11,587,431,644	33,125,831,259	20,813,899,424	–	72,431,923,465
Other borrowings	20,299,717,968	1,903,296,614	1,564,984,548	4,975,918,485	11,855,518,321	–	20,299,717,968
Debt securities issued	1,014,034,248	–	–	1,014,034,248	–	–	1,014,034,248
Subordinated term debts	4,210,565,525	–	–	10,243,764	4,200,321,761	–	4,210,565,525
Interest bearing liabilities	97,956,241,206	8,808,057,752	13,152,416,192	39,126,027,756	36,869,739,506	–	97,956,241,206
Interest rate sensitivity gap	6,451,213,793	402,170,682	(1,304,342,625)	(27,028,588,261)	28,359,653,308	6,022,320,689	6,451,213,793

	If market interest rate go up by 1% effect to interest Income	If market interest rate drop by 1% effect to interest Income
Effect on rate sensitive assets	1,044,074,550	(1,044,074,550)
Effect on rate sensitive liabilities	(979,562,412)	979,562,412
Sensitivity of profit or loss	64,512,138	(64,512,138)

Asset or liability	Interest rate sensitivity assets and liabilities as at 31 December 2018						
	Carrying amount LKR	On demand LKR	1-3 Months LKR	3-12 Months LKR	over 1 Year LKR	Non-interest LKR	Total LKR
Cash and cash equivalents	4,171,938,630	301,146,575	–	–	–	3,870,792,055	4,171,938,630
Placements with banks	9,528,425,565	6,100,000,000	3,250,000,000	178,425,565	–	–	9,528,425,565
Loans and receivables to other customers	77,507,021,162	3,040,896,001	2,813,966,720	11,358,518,596	58,256,775,070	2,036,864,775	77,507,021,162
Interest bearing assets	91,207,385,357	9,442,042,576	6,063,966,720	11,536,944,161	58,256,775,070	5,907,656,830	91,207,385,357
Due to other customers	67,474,821,535	6,322,925,433	9,729,321,198	31,544,542,057	19,878,032,847	–	67,474,821,535
Other borrowings	15,420,967,962	282,415,255	1,791,301,041	4,147,422,945	9,199,828,722	–	15,420,967,962
Debt securities issued	4,198,547,716	3,035,440,000	–	198,547,716	964,560,000	–	4,198,547,716
Subordinated term debts	1,008,027,823	–	–	15,058,060	992,969,763	–	1,008,027,823
Interest bearing liabilities	88,102,365,036	9,640,780,687	11,520,622,239	35,905,570,778	31,035,391,332	–	88,102,365,036
Interest rate sensitivity gap	3,105,020,321	(198,738,111)	(5,456,655,519)	(24,368,626,617)	27,221,383,738	5,907,656,830	3,105,020,321

	If market interest rate go up by 1% effect to interest Income	If market interest rate drop by 1% effect to interest Income
Effect on rate sensitive assets	912,073,854	(912,073,854)
Effect on rate sensitive liabilities	(881,023,650)	881,023,650
Sensitivity of profit or loss	31,050,203	(31,050,203)

Equity price risk

Equity price risk is the risk that the fair value of equities decreases as the result of changes in the level of equity indices and individual stocks. The non-trading equity price risk exposure arises from equity securities classified as fair value through other comprehensive income.

43 Capital

The Bank maintains an actively managed capital base to cover risks inherent in the business. The adequacy of the bank's capital is monitored using, among other measures, the rules and ratios established by the Basel Committee on Banking Supervision (BIS rules/ratios) and adopted by the Central Bank of Sri Lanka.

During the past year, the Bank had complied in full with all its externally imposed capital requirements.

Capital management

The primary objectives of the Bank's capital management policy are to ensure that the Bank complies with externally imposed capital requirements and that the Bank maintains strong credit ratings and healthy capital ratios in order to support its business and to maximise shareholder value.

The Bank manages its capital structure and makes adjustments to it in the light of changes in economic conditions and the risk characteristics of its activities. In order to maintain or adjust the capital structure, the Bank may adjust the amount of dividend payment to shareholders, return capital to shareholders or issue capital securities.

44 Comparative reclassification

The presentation and classification of following item in these financial statements are amended to ensure comparability with the current year.

Accounting Policy

The accounting policies have been consistently applied by the Bank with those of the previous financial year in accordance with the Sri Lanka Accounting Standard – LKAS 1 on "Presentation of Financial Statements" Comparative information is reclassified wherever necessary to comply with the current presentation. The presentation and classification of the following items in these financial statements are amended to ensure the comparability with the current year.

	As disclosed in previous year (2018)	Classification	As disclosed in this year (2019)
Statement of comprehensive income			
Interest income	13,116,781,577	30,005,579	13,146,787,156
Net fee and commission income	222,370,769	(30,005,579)	192,365,190
Statement of financial position			
Defined benefit liability	–	354,854,450	354,854,450
Other liabilities	1,122,687,852	(354,854,450)	767,833,402

The above reclassification did not have any impact on Statement of Comprehensive Income, earnings per share, operating, investing and financing cash flows for the year ended 31 December 2018.