



Securities and Exchange Commission of Sri Lanka

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Mission Statement

“To Promote, Develop and Maintain a Securities Market that is Fair, Efficient, Orderly, and Transparent”.

Members of the Commission



Mr. M L Mack
Chairman
(from February 2002)



Dr. Nihal Jinasena
Commission Member

A black rectangular box with the text "MEMBERS OF THE COMMISSION" in white, bold, uppercase letters.



Mr. P M Nagahawatte
Commission Member



Mr. D K Hettiarachchi
Commission Member



Mr. A D B Talwatte
Commission Member



Mr. Faiz Mohideen
Commission Member



Mr. L C R de C Wijetunge
Commission Member



Mr. Hemaka Amarasuriya
Commission Member



Mr. G C B Wijeyesinghe
Commission Member
(from February 2002)

**MEMBERS OF THE
COMMISSION**



Mr. W R Johnson Peiris
Commission Member
(from September 2002)



Mrs. Dayani de Silva
Commission Member
(until February 2002)

Principal Officers of the Secretariat



Dr. Dayanath C Jayasuriya
Director General



Mrs. L S A Seresinhe
Director, Corporate
Affairs



Mr. Benildus P Tissera
Director, Supervision



Mr. Dhammika Perera
Director, Investigations &
Monitoring



Mr. Kithsiri Gunawardena
Director, Legal &
Enforcement



Mr. Malik Cader
Director, Public Relations
& Market Development



Ms. Ianthie Jayaratne
Director, Finance &
Administration

Chairman's Review

After a period of relative inactivity, interest in the Stock Market was a welcome change during the year under review. As Sri Lanka laid the foundation for a new era of peace and stability, investor confidence was evident from active trading in the Colombo Stock Exchange and a marked improvement in prices. A possible contributory cause is the new deregulated regulatory environment—as was reported in last year's Annual Report, the Securities and Exchange Commission (SEC) undertook, in 2001, a major review of the complex regulatory regime that had evolved over a period of approximately 15 years.

Many unnecessary and cumbersome regulatory requirements were repealed and procedures in place were streamlined. The process of review and consultation continued this year as well with significant changes being made, *inter-alia*, to the Unit Trust Code.

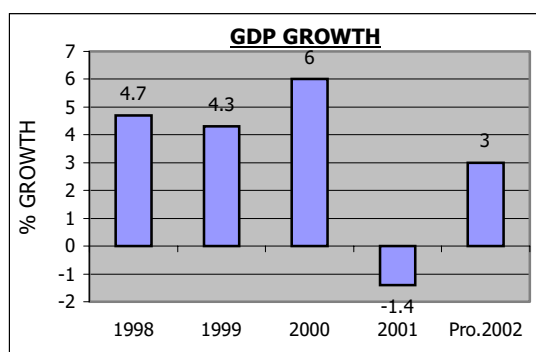
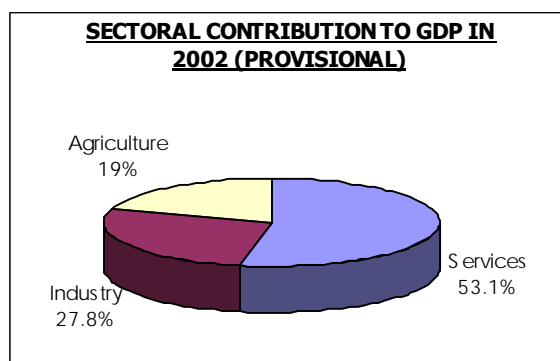
During the year under review, the SEC intensified its involvement in international activities. It signed Memoranda of Understanding with Australia and New Zealand and participated in several IOSCO sponsored activities. Sri Lanka was unanimously chosen to host, for the first time, the IOSCO's Asia Pacific Regional Committee (APRC) Meeting and the Law Enforcement Directors' Meeting in January 2003. More importantly, Sri Lanka's bid to host the IOSCO's Annual Conference in 2005 was successful. We acknowledge, with gratitude, the confidence the international community has thus placed in the SEC and our country.

This advance copy of the Annual Report for the year 2002 is being released on the occasion of the IOSCO's APRC Meeting. We hope that its contents will provide useful insights into how a securities market regulatory body in an emerging market operates.

An Overview of the Performance of the Sri Lankan Economy

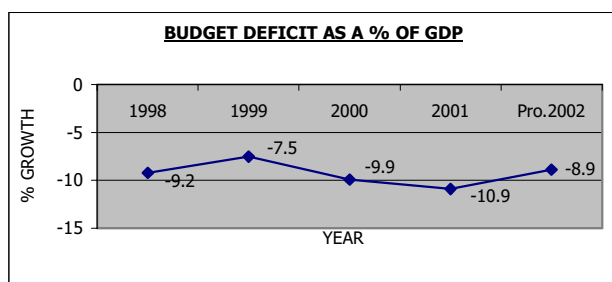
The performance of the Sri Lankan economy showed signs of recovery in 2002. The factors which contributed to the recovery include the cessation of hostilities, improved business confidence, decline in the rate of inflation and interest rates, and stability in the exchange rate.

The GDP grew by 2.7% on a cumulative basis during the first three quarters of 2002 and by 5.3% in the third quarter. This quarterly growth of 5.3% was the highest recorded since the third quarter of 2000. This is an improvement on the reduction in GDP by 1.4% in 2001. The government envisaged an annual growth rate of approximately 3% for 2002. The services sector which accounts for more than half of GDP grew by 8%, the industry sector which contracted during the first half of the year grew by 3.1% and the agriculture sector grew by 1.2% in the third quarter of 2002 compared with the corresponding period of the previous year.



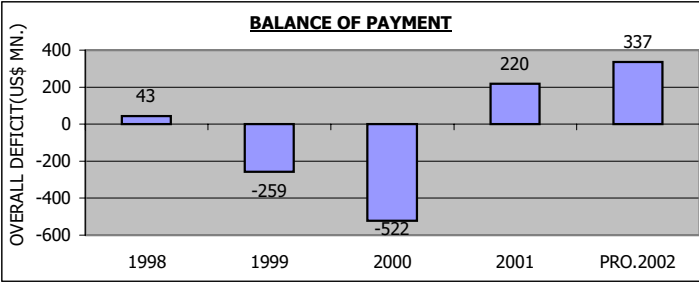
The inflation rate has declined from more than 14% to approximately 10% this year. This reflects the benefits of increasing domestic agricultural output, and lighter pressure from import prices (except for petroleum). The net impact of the VAT introduced in 2002 is expected to reduce market prices of many basic consumer items.

The Finance Minister in his budget speech 2002 proposed several reforms in taxation, expenditure and public debt management. Accordingly, several taxes were abolished and GST and NSL were consolidated into a single VAT. The overall budget deficit in 2002 is estimated to rise approximately to 8.9% of GDP in comparison with the original target of 8.5% of GDP. This is a result of the current account deficit declining by 2.3% of GDP due to a significant shortfall in revenue and expenditure on interest payments. As in the previous year, the government's outstanding debt stock is expected to increase to 57.3% of GDP at a faster rate than the rate of growth in nominal GDP. The privatization programme is expected to raise Rs.21 billion. This will mainly be from the divestiture of Sri Lanka Insurance Corporation and the sale of the balance shares of Sri Lanka Telecom. The privatization programme will continue in 2003.



The overall performance in the external front improved and an overall surplus of US dollars 337 million is expected in 2002. Lower imports, high inflows, under remittances and the capital account contributed to this surplus. Export earnings declined by 2% in 2002 as against 12.8% in 2001. This was attributable to both lower prices and volumes of exports. Expenditure on imports is estimated to increase by 2% over that in 2001. As a result, the annual trade deficit is expected

to increase to US dollars 1,345 million in 2002. Foreign direct and portfolio investments have a potential likelihood to increase, reflecting the impact of improving investor confidence. An increase in gross official reserves is expected to increase to a level that is sufficient to cover 3.6 months of imports.

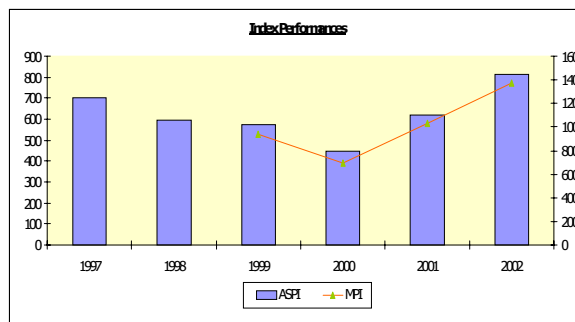


The gradual decline in interest rates on fixed income securities and improved business confidence due to progress made in the peace process led to active participation of both domestic and foreign investors. Thus the stock market became one of the best performing markets in the world.

Equity Market - 2002

Activity at the Colombo Stock Exchange increased significantly reflecting the gradual economic recovery during the year 2002. The Colombo Bourse gained 31.2% this year and became one of the best performing Stock Markets in the world. The signing of the Ceasefire agreement in February between the government and separatist rebels led to a gradual increase in both indices during the first quarter of 2002. The upward movement continued throughout the year. The market was driven mainly by local investors. With the positive signs of the peace process the CSE was able to attract many foreign investors.

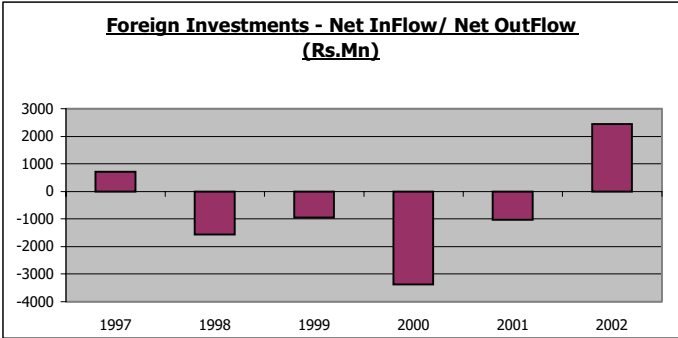
The All Share Price Index (ASPI) which opened the year at 621.0 points closed the year at 815.1 points in December 2002. This is an increase of 31.2%. The MILANKA Price Index (MPI) opened the year at 1,031.0 points and closed at 1,374.6 points gaining 33.3%. Both indices recorded new highs for the year 2002 during the month of March. The ASPI recorded its highest point 645.1 on 22 March 2002 while MPI recorded its highest point 1,055.0 on the same day prior to the budget proposals. The ASPI recorded a five year high of 860.3 on 26 September 2002 and the MPI which was introduced in January 1999, recorded its highest ever point of 1,479.8 on the same day as a result of the decision taken by the Defence Minister to lift the ban on the LTTE and the completion of the first round of peace talks. Market Price Earnings ratio increased to 12.1 from 7.5 at the end of the previous year.



The levels of trading volumes increased significantly during 2002. The annual turnover at the Colombo Stock Exchange was Rs. 30.5 billion with an average daily turnover of Rs 128 million, second only to the CSE's best ever total turnover of Rs. 34 billion and an average daily turnover of Rs. 147 million achieved in 1994. A total turnover of Rs. 5.2 billion was recorded during the month of June, the third highest total turnover for a month since March 1994. The average daily turnover for June was Rs. 273.9 million. This is the second highest average daily turnover recorded for a month in the history of the CSE. The increase in turnover in June was due to strategic buying.

YEAR	TOTAL TURNOVER (Rs Mn)	AVERAGE DAILY (Rs Mn)	SHARES TRADED (No Mn)	TRADES (No)
1997	18,315	76	515	206,312
1998	18,232	76	634	329,068
1999	14,842	61	486	205,759
2000	11,049	46	449	160,277
2001	14,057	58	747	159,723
2002	30,523	128	1,220	283,126

The CSE introduced a new sector, Information Technology, in May 2002. There were nine new listings during the year. The Initial Public issues i.e Apollo Hospitals Ltd, Tess Agro Ltd and Sri Lanka Telecom Ltd were oversubscribed soon after their launches. A total of Rs. 4.2 billion was raised through the CSE new issues as well as other rights issues. Interest rates on fixed income securities declined during the year. The economy showed signs of recovery and this led to total capital inflows of Rs 7.4 billion (Foreign sales amounted to Rs 5 billion). In the year 2002 after the lapse of four years foreigners were net buyers and net foreign inflow of Rs 2.4 billion was recorded compared to the net foreign outflow of Rs 1.02 billion in 2001. Foreign participation accounted for 24.5% of the total purchases at the end of the year 2002. The highest net foreign inflow for the year was Rs 765 million in the month of May.



Sector performances showed the market sentiments with 15 sectors recording gains while the IT, Oil Palms and plantations sectors declined. The withholding tax of 10% on investor returns, the introduction of 10% VAT on net profits on banks and other financial services and the 0.1% debit tax across all bank accounts did not contribute to active trading in the banking sector. Nevertheless, the Bourse buoyed by strategic buying which mainly revolved round the

manufacturing, banking, diversified tourism and hotels sectors. The banking sector recorded a profit growth of 100%, hotels and travels 300% and diversified holdings 200%.

Corporate Affairs Division

CORE FUNCTIONS

- ▶ Examine financial statements of companies with reference to compliance with relevant laws and regulations on “true and fair” disclosure.
- ▶ Monitor market activity to detect and prevent market abuse.
- ▶ Promote Corporate Governance Practices.
- ▶ Inquire into and resolve complaints of market intermediaries and investors.
- ▶ Verify the accuracy of the notices/announcements published by issuers.
- ▶ Monitor compliance with the Companies’ Takeovers and Mergers Code 1995.
- ▶ Process and approve off-the-floor share transactions.
- ▶ Respond to surveys conducted by IOSCO.
- ▶ Process and approve the de-listing applications.

KEY ACTIVITIES

Review of Annual Reports

All Listed Companies are required to submit annual reports within six months of the end of the financial year to their shareholders and the Colombo Stock Exchange. The audited accounts should be prepared and presented in accordance with the Sri Lanka Accounting Standards. The annual reports must comply with the relevant legal provisions.

During the period under review, the Division reviewed Annual Reports of Listed Companies to ascertain the degree of compliance with the SEC Act, CSE Rules, Sri Lanka Accounting Standards (SLAS) and relevant provisions of the Companies Act.

The objective of the exercise was to enhance the quality of annual reports and accounts issued by Listed Companies, as the quality of information contained in these reports has a direct impact on investor decision-making and confidence placed in the Securities Market. These efforts also facilitated the Commission in researching the degree of comparability of financial statements produced by Listed Companies, in addition to timeliness and relevance of information contained in them.

The Listed Companies are required to disseminate material information promptly in order to establish much needed transparency in the Securities Market and ensure that the professional standards are maintained.

The Division reviewed interim accounts, market disclosures and other information that listed companies are required to disseminate to the public as a part of their continuing listing obligations.

The review of Annual Reports and Accounts focused on the following areas:

- Compliance with Colombo Stock Exchange (CSE) Rules
- Compliance with Sri Lanka Accounting Standards (SLAS)
- Compliance with Companies Act Requirements and other relevant legislation

Corporate Governance Practices
 Shareholder and Investor Information
 Financial Summary
 Chairman's Report
 Report of the Directors
 Report of the Auditors
 Financial Highlights
 Corporate Information
 Management Discussion and Analysis

The Division reviewed approximately 100 Annual Reports and Accounts of Listed Companies and communicated with 50 companies on matters relating to non-compliances with relevant rules and regulations. Action was taken on non-compliances considering the nature and the materiality of the issues. The responses of Listed Companies were extremely positive to this endeavour. In most instances, the SEC cautioned the companies to ensure that such deviations were not repeated in future annual reports and accounts. This process has contributed to improving the level of awareness of companies and auditors regarding the obligations placed upon them in the preparation and presentation of annual reports and accounts.

In addition, the SEC forwarded a report on its findings to the Institute of Chartered Accountants of Sri Lanka for information and necessary action.

Key Areas of Non Compliance with Sri Lanka Accounting Standards

RELEVANT SLAS	NO. OF COMPANIES NOT COMPLIED	AREAS OF NON COMPLIANCE	NUMBER OF NON COMPLIANCES
SLAS 3 Presentation of Financial Statements	48	Accounting policies	21
		Directors' responsibility	23
		Right, preferences and restrictions of shares	14
		Nature and purpose of reserves	21
		Inadequate cross references	26
		Sub classifications of the line items presented	03
SLAS 5 Inventories	13	Amount of inventories pledged	07
		Cost formula used	06
SLAS 14 Accounting for Taxes on Income	33	Tax Reconciliation	25
		The amount of Tax Losses	10
SLAS 16 Retirement Benefit Costs	25	Defined Contribution Plans	24

SLAS 18 Property, Plant & Equipment	30	Amounts of restrictions on title & Property, Plant & Equipment pledged as securities	18
		Details of revalued assets	17
SLAS 21 The Effects of Changes in Foreign Exchange Rates	10	Exchange differences	10
SLAS 22 Accounting for Investments	05	Market value of marketable investments	05
SLAS 25 Business Combinations	11	Details of Goodwill and negative Goodwill	10
SLAS 28 Reporting Financial Information by Segment	15	Financial information by segments	15
SLAS 30 Related Party Disclosures	28	Elements of Related Party Transactions not disclosed	28
SLAS 31 Financial Reporting of Interest in Joint Ventures	02	Aggregate amount of current assets, long term assets, current liabilities and long term liabilities, income and expenses relating to its interest in joint ventures	02
SLAS 33 Revenue Recognition and Disclosure in the Financial Statements of Finance Companies	04	Maturities of Assets and Liabilities	02
		Concentration in the distribution of assets	03
		The amount of non performing loans and the basis of calculation of same	04

Corporate Governance

In year 2001 the SEC requested all Listed Companies to disclose in their annual reports procedures adopted with regard to Best Practices in their corporate environment. Consequently, there was a significant increase in the number of companies complying with this requirement.

It was noted that only a few companies made extensive disclosures in their annual reports regarding the corporate governance practices adopted during the year, whilst a majority included a brief statement. The SEC encouraged listed companies to concentrate on the following subject areas when adopting Best Practices in their organisations:

- The structure, key functions and activities of the Board
- Board meetings- what they do, how they function and frequency of meetings
- What authority the Board delegates and to whom
- Matters that require disclosure
- Audit Committee reports and functions of other committees such as Credit Risk Committee and Human Resources Committee.

During the year under review the Division undertook a study on Corporate Governance Practices adopted by Listed Companies. To facilitate this study the following information was obtained:

- The number of Executive Directors and Non-executive Directors appointed to serve on the Board;
- Whether an Audit Committee has been appointed, and, if so, the number of Executive Directors and Non-executive Directors serving on the Committee; and
- Whether a Remuneration Committee has been appointed and if so, the number of Executive Directors and Non-executive Directors serving on the Committee.

The information collected was provided to the Committee appointed by the SEC to examine the Role of the Auditors. The highlights of the study were as follows:

- 13% listed companies had less than 30% of Non-Executive Directors serving on the Boards;
- 23% of listed companies had between 30% to 50% Non-Executive Directors serving on the Board;
- 64% of the listed companies had more than 50% of Non-Executive Directors serving on the Board.

Further, it was revealed that 45% of listed companies had Audit Committees and 25% of listed Companies had Remuneration Committees.

However, the survey did not include a study to verify the “independence” of the Non-Executive Directors.

Takeovers and Mergers

There were 6 Takeovers during the year under review and the Division ensured due compliance with the Takeovers and Mergers Code by the parties concerned. Details of these Takeovers and Mergers are set out in Table A.

One mandatory offer and one voluntary offer failed since the shareholders of the offeree companies did not accept the offer. The other offers were successfully completed. Several complaints and inquiries received regarding the offers were resolved. In one instance, namely Kapila Heavy Equipments Limited, the offeror defaulted in making payment and the SEC is in the process of filing action against the offeror for violating the Takeovers and Mergers Code.

TABLE A

Offeror	Sector	Offeree	Type of Offer
Mr Gamini Fonseka	Construction & Engineering	Kapila Heavy Equipments Ltd.	Mandatory
Master Divers (Pvt.) Ltd.	Manufacturing	Pelwatte Sugar Industries Ltd.	Mandatory
Asia 2000 Investment Inc.	Land & Property	East West Properties Ltd.	Mandatory
Pacific Far East Investments Incorporated	Land & Property	Infrastructure Developers Ltd.	Mandatory
Mr K D D Perera	Hotels & Travels	Connaissance de Ceylan	Mandatory
Mr R Nanayakkara	Bank, Finance & Insurance	Lanka Orix Leasing Company	Voluntary

Approval of Off- the-Floor Share Transactions

During the year under review the Division approved approximately four hundred exceptional private transfers. These transfers were effected in order to facilitate margin trading, fund management, de-listing and restructuring.

Handling of Complaints

The Division received 35 complaints from shareholders of Listed Companies. Out of these 3 were outside the jurisdiction of the SEC.

The details of the complaints and their status as at 31 December 2002 are given in Table B.

TABLE B

NATURE OF COMPLAINT		TOTAL NO. OF COMPLAINTS	PENDING AS AT 30/11/02
1	Share certificates / debenture certificates/ and related issues	7	-
2	Disclosure requirements/misleading financial information / issues in relation to financial statements	7	-
3	Complaints against Stockbrokers	1	-
4	Non-payment of dividends/rights/ compensation / interest to shareholders	5	2
5	Takeovers and Mergers Code	3	-
6	Delisting of Companies	3	-
7	Insider Dealing	1	-
8	Miscellaneous	5	-
TOTAL		32	2

Market Monitoring

The SEC monitors trading of listed securities on the Stock Exchange for unusual price and volume movements on the Exchange using a real time computer assisted surveillance system.

The Division also scrutinizes newspaper articles, verifies rumors and advertisements on a daily basis to identify any possible breaches of securities laws and regulation. The surveillance staff monitors the share movements for indications of market manipulations and/or insider dealing.

When an unusual trading pattern is identified, the Division analyses all material related to the issue to decide whether further investigation is warranted by the Investigations Division.

During the year the surveillance staff examined 22 issues of which details are given below:

NATURE OF SURVEILLANCE	NO OF ISSUES	ACTION TAKEN
Takeovers and Mergers	06	Disclosures as per the Takeovers and Mergers Code were required to be made.
Heavy Trading/ Unusual Trading Pattern	13	Having initiated several queries nine investigations were terminated due to lack of evidence; other matters were transferred to the Investigations Division.
References from newspaper reports.	03	Observations of the parties concerned were called for. No further action was required.

The Corporate Affairs Division and the Monitoring Division were integrated in the latter part of the year.

Other Matters

- The SEC is a member of the International Organization of Securities Commissions (IOSCO). During the year under review, the Division responded to several questionnaires forwarded by IOSCO. The surveys covered the following matters:
 - a) Principles relating to Collective Investment Schemes
 - b) Principles relating to Market Intermediaries
 - c) Principles relating to Secondary Market
 - d) Survey on Investor Protection

- A team of IMF/World Bank representatives conducted an assessment of the Sri Lanka securities market. The assessment was conducted with regard to the following two subject areas:
 - o Practices on Transparency in Good Monetary and Financial Policies-Securities Regulations.
 - o Assessment of compliance with IOSCO's Objectives and Principles for Securities Regulations.

The IMF/World Bank Financial Sector Assessment Mission Team expressed great satisfaction with the current state of the regulatory system. However, the team recognized the need for a formal Memorandum of Understanding with the Central Bank to enhance transparency in formulating and reporting of Financial Policies. The team also recommended that SEC publishes its own internal governance procedures and code of conduct. The team took note of the fact that the Sri Lankan authorities have taken steps to rectify certain shortcomings in the legislation, primarily through the proposed amendments to the SEC Act.

During the year under review the Division reviewed 5 de-listing applications in terms of the relevant Rules. The new de-listing Rules which came into effect in December 2001 provide a fast track procedure to process de-listing applications. The primary objective is to ensure that the interests of shareholders are protected. With the intervention of the SEC, the price paid to dissenting shareholders who wish to sell their shares was increased in some of the instances.

Investigations Division

CORE FUNCTIONS

- ▶ Deal with complaints that appear to require the institution of legal or other proceedings or the imposition of sanctions;
- ▶ Conduct investigations into fraudulent activities in the securities market and violations of securities laws and regulations;
- ▶ Conduct inquiries with regard to proposed takeovers and mergers where it is alleged that the mandatory offer provisions contained in the Takeovers & Mergers Code have been triggered; and
- ▶ Conduct training programmes on securities related investigations.

KEY ACTIVITIES

The Division conducted a total of nineteen investigations in the year 2002, out of which fourteen were completed during the year. The details and a brief description of the action taken/current status of the said investigations are given below:

NATURE OF INVESTIGATIONS	NUMBER OF INVESTIGATIONS	ACTION TAKEN/CURRENT STATUS
Insider Dealing ¹	03	Consequent to detailed investigations, two cases were terminated due to the lack of evidence to establish charges of Insider Dealing, whilst the other investigation was pending.
Takeovers & Mergers	03	Consequent to a detailed investigation, the cases were terminated since the Mandatory Offer provisions contained in the Takeovers & Mergers Code had not been triggered by any party connected to the investigations.
Inquiries into the Business Affairs of Listed Companies	03	Two investigations were terminated due to the evidence /material elicited during the investigations not revealing any contravention of the provisions of the Securities laws, rules and regulations. As at the end of the year under review, one investigation was on-going.
Investor and Other Complaints	07	Investigations were terminated in five cases due to the non- availability of evidence to prove the allegations contained in the complaints. One investor complaint was resolved and another investigation was pending at the end of the year. One of the complainants providing the SEC with false and misleading information during its inquiry has led to Notice of Action being sent by the SEC to the said person prior to the institution of proceedings.
Market Manipulation ²	01	Investigation is on-going.
Front Running ³	01	Investigation is on-going.

¹ Insider Dealing - Trading in the shares of a listed company whilst in the possession of unpublished price sensitive information in respect of the securities of the said Company.

² Market Manipulation – Creation of a false or misleading appearance in respect of the trading or the price of any securities listed in a stock market.

³ Front Running – Execution of trades whilst having the knowledge of the orders to be executed, with the intent of making available the shares to the prospective investors at a profit.

The investigative powers vested in the Secretariat by the Securities and Exchange Commission Act have proved to be inadequate. This has been a major impediment towards carrying out investigations effectively. Measures were taken to propose amendments to the SEC Act to augment the investigative powers with the intent of empowering the Commission to summon witnesses, record statements, visit premises, inspect and take copies of records etc. The aforesaid proposed amendments have already been approved by the Cabinet and forwarded to the Parliament for approval. The acquisition of such powers by the SEC will enhance the ability of the Investigations Division to conduct investigations in a more efficient and comprehensive manner.

Legal and Enforcement Division

CORE FUNCTIONS

- ▶ Provide legal support and advice to the Commission and the various divisions of the Secretariat.
- ▶ Review, suggest and draft amendments to the Securities and Exchange Commission of Sri Lanka Act and subordinate legislation made thereunder.
- ▶ Review and approve rules and regulations of the Colombo Stock Exchange.
- ▶ Process applications relating to the licensing of the Stock Exchange and the Stock brokers.
- ▶ Handle litigation with regard to prosecuting persons who contravene the provisions of the SEC Act, and liaise with the Attorney General's Department, other counsel, and Legal Draftsman's Department on relevant matters.
- ▶ Present matters at inquiries before the Commission.

KEY ACTIVITIES

During the year under review, the Legal and Enforcement Division, amongst other things, handled matters relating to the renewal of the licences of 15 Stock Brokers, pending cases, inquiries and amendments to the SEC Act and the CSE Rules.

A. CASES FILED BY THE SEC

1. SEC vs. Magpek Exports Ltd. and its Directors

The SEC filed charges against the above company and its Directors for not immediately disclosing to the market certain material information to prevent the creation of a false market for shares of Magpek Exports Ltd. as required by the SEC Rules. The case was laid by pending the decision of the Supreme Court in the case of SEC vs. Kotagala Plantations Ltd.

Having received the Supreme Court order in the SEC vs. Kotagala Plantations case the SEC reopened the case in the Magistrate's Court.

Subsequently charges against three of the defendants were compounded on an application made by their counsel to the SEC. The trial against the remaining defendants was pending as at 31st December 2002. (Refer item D)

2. SEC vs. Gihan Rajapakse (see item A 3 below)

3. SEC vs. Vajira Premawardena

The SEC initiated an investigation into certain significant increases in the share prices of certain companies listed on the CSE, which occurred during the latter part of December 1998.

The said investigation revealed that Mr. Rajapakse and Mr. Premawardena, two Fund Managers, had been responsible for making the investment decisions pertaining to the purchase of shares in certain companies during the aforesaid period into the securities account of NDB and CTC Eagle which accounts were managed by Eagle NDB.

The investigation further revealed that the said purchases were manipulative in nature and resulted in a significant increase in the share price of the companies.

The SEC filed charges in the Fort Magistrate's Court on 24 January 2000 against the above two Fund Managers.

An objection was raised on the ground that the charges could not be sustained, as the rules were not valid. However the Magistrate overruled the said objection and the case was fixed for trial. A Revision Application was thereafter filed in the High Court of Colombo against the decision of the Magistrate. Prior to the order on the Revision Application being delivered by the High Court an application was made by Mr. Rajapakse and Mr. Premawardena to the SEC to compound the charges against them. The case was compounded and the charges against them were withdrawn by the SEC upon Mr. Rajapakse and Mr. Premawardena withdrawing the revision applications filed in the High Court and Rs 50,000/- each being paid to the Compensation Fund. (Refer item D)

B. CASES FILED AGAINST THE SEC

1. Sampath Bank Limited vs. SEC & nine others

Upon an investigation conducted by the SEC, it was revealed that certain parties acting in concert had exceeded the threshold limit specified in Rule 31 of the Takeovers & Mergers Code in relation to the shares of Sampath Bank Ltd., a company listed on the Colombo Stock Exchange. The SEC called upon the five companies and two individuals— parties deemed to have acted in concert - to make a mandatory offer as required by the Takeovers and Mergers Code on or before the time specified in the said Rule 31.

Thereafter the SEC received summons to file answer in the District Court case filed by Sampath Bank Ltd. against the Defendants. The first to the seventh Defendants are the parties that were called upon by the SEC to make the mandatory offer. The SEC, the Colombo Stock Exchange and the Central Depository System (Pvt) Ltd. were named as the 8th, 9th and 10th Defendants respectively.

On 20th July 2000, the District Judge issued an order against the SEC restraining the approval of an offer document in relation to a mandatory offer the 1st to 7th Defendants were called upon to make in terms of the Takeovers and Mergers Code 1995. The case was pending at the end of the year.

C. INQUIRIES PENDING BEFORE THE SECRETARY, MINISTRY OF FINANCE

City Investments Ltd.

The SEC received a complaint with regard to a delayed payment by City Investments Services Ltd. (CISL) a licensed member of the CSE in respect of 11,347 shares of E.B. Creasy Ltd. The Complaints Committee in consultation with the Attorney General and on a report submitted by the Examiner of Questionable Documents came to a finding that the Broker

had willfully tendered transfer documents in respect of the above shares with the forged signature of the client in order to obtain payment. The SEC acting under section 21(1) (d) of the SEC Act, suspended the licence issued to City Investments Services Ltd. with immediate effect. Thereafter City Investments Services Ltd. appealed to the Secretary, Ministry of Finance who confirmed the decision of the Commission. Later an appeal was made to the Court of Appeal by CISL. The Court of Appeal ordered the Secretary to hold a proper inquiry by giving the Petitioner a hearing and to make a decision according to law. CISL has not pursued the appeal. Its licence issued by the CSE has not been renewed.

The counsel for CISL approached the Commission to explore the possibility of its appeal being withdrawn in the event the CSE renewed its licence. The matter of the renewal of the licence was pending at the end of the year.

D. CASES COMPOUNDED BY THE SEC

1. SEC vs. Magpek Exports Ltd. and its Directors

Case referred to in item A(1) above.

A request was made by 3 directors of Magpek Exports Ltd. namely, Mr Piyasiri Ratnayake, Mr Tennyson Rodrigo and Ms Deemathi de Silva to compound the charges against them. Accordingly the case was compounded by the SEC for a sum of Rs 500,000 to be paid by each director to the Compensation Fund in terms of Section 51A of the SEC Act as amended.

2. SEC vs. Gihan Rajapakse(see item D 3 below)

3. SEC vs. Vajira Premawardena

Cases referred to in item A2 & 3 above.

Mr. Rajapakse and Mr. Premawardena made a request to the SEC to compound the charges against them. Having considered the circumstances in which the violation was alleged to have occurred the SEC compounded the charges against them for a sum of Rs.50,000/- each in terms of Section 51(A) of SEC Act and the proceeds were credited to the Compensation Fund.

E. AMENDMENTS TO THE SEC ACT NO. 36 OF 1987

The amending legislation to the SEC Act has been finalized and was forwarded to the Ministry of Finance for submission to the Cabinet of Ministers. The proposed amendments seek to-

- grant wider powers of investigation to the Commission in all matters where the Act and the rules and regulations made thereunder are suspected to have been violated;
- widen the scope of the insider dealing provisions and the penalties thereon;
- widen the punitive jurisdiction of the Commission;
- widen the powers pertaining to listing and quotations;
- repeal the provisions relating to the appellate powers granted to the Secretary to the Ministry of Finance;

- register new market intermediaries, namely underwriters, margin providers, credit rating agencies, the Central Depository Systems, and investment managers in so far as listed portfolios are concerned.

Further the SEC has recommended that statutory protection should be provided in the proposed amendments in order to protect the Members of the Commission and Staff of the Secretariat against contempt.

F. REVISION TO THE UNIT TRUST CODE 1995

The Unit Trust Code 1995 was revised and the revised draft was forwarded to the Legal Draftsman's Department for approval.

G. COLOMBO STOCK EXCHANGE RULES

The Division examined and recommended to the Commission the following CSE Rules subject to certain amendments:

- Amendments to the Listing Rules of the Exchange.
- Rules for Acknowledgement of Debt.
- Amendments to the Member Regulations of the CSE.
- Amendments to the Automated Trading Rules of the CSE.
- Amendments to the Central Depository System Rules of the CSE.
- Amendments to the Memorandum and Articles of Association of the CSE.

H. DEMUTUALISATION OF THE COLOMBO STOCK EXCHANGE (CSE)

The licence of the Colombo Stock Exchange was renewed for a further period of three years during the year 2001. However the CSE was requested to implement arrangements for demutualisation of the Exchange during this period of three years. The SEC and the CSE have sought the assistance of consultants.

I. MEMORANDUM OF UNDERSTANDING (MOU) IN RELATION TO ASSISTANCE AND MUTUAL COOPERATION

The SEC signed MOU's with the Securities Commission of Malaysia, the Capital Market Supervisory Agency of Indonesia, the Australian Securities and Investments Commission and the Securities Commission of New Zealand.

J. MISCELLANEOUS

- Notice of Action was issued in respect of three listed companies for non-disclosure of material information and two of them were issued with letters of warning.
- A Committee was appointed to examine the issues relating to revision of staff trade rules, requirement of a public float and deregulation of brokerage commission.
- Proposals were made to amend the Companies Act.
- Approval of regional and country funds in compliance with the criteria laid down in the Gazette Extraordinary No. 720/12 of 24th June, 1992 pertaining to investment by non-residents in companies incorporated in Sri Lanka.
- Amendments made to Rule 31 of the Takeovers and Mergers Code 1995 were forwarded to the Legal Draftsman's Department for approval.

Supervision Division

CORE FUNCTIONS

- ▶ Monitor the financial and operational performance of licensed Stockbrokers and Management Companies of Unit Trusts.
- ▶ Conduct on-site inspections of Stock Broking Companies and Management Companies of Unit Trusts in order to ensure that adequate capital is maintained and these Companies are financially stable.
- ▶ Ensure that Stockbrokers employ competent staff to conduct business.
- ▶ Conduct regulatory audits of the Colombo Stock Exchange (CSE).
- ▶ Ensure that laws and regulations of the SEC are duly complied with by Stockbrokers and Management Companies of Unit Trusts.
- ▶ Investigate complaints made by investors with regard to the Central Order Desk (COD) Procedure on the execution of orders.

KEY ACTIVITIES

Supervision of Stock Broking Companies

The SEC Act requires all Stock Broking firms to obtain a licence annually and to be members of a licensed Stock Exchange. During the year 2002, there were fifteen Stock Broking Companies. The number has remained unchanged since 1994.

The SEC in order to pursue the objective of monitoring the financial and operational performance and financial stability of licensed Stock Broking Companies, requires that the Stock Broking firms maintain a minimum net capital requirement¹ of Rs. 5 million effective from 7th March 2001. In addition to the minimum net capital requirement, Stock Broking Firms are required to maintain a specified liquidity requirement; appoint competent compliance officers capable of overseeing regulatory compliance procedures; maintain separate client accounts and follow an established COD Procedure pertaining to the receipt, execution, and allocation of orders. The Stock Broking Companies are required to submit monthly unaudited accounts and Compliance reports to the Commission. These reports are reviewed by the officers of the Supervision Division to ensure that the compliance procedures are adhered to and the unaudited accounts are used to monitor and compare the performance of the Broking industry.

All fifteen Stock Broking firms were visited at least once to ensure that the companies were financially stable and that they complied with the COD Procedure. During December 2001, the SEC and CSE reached an understanding that the COD Procedure during on-site inspection would only be verified if an investor lodged a complaint. This decision was based on the representations made by the Stock Brokers through the Stock Brokers' Association due to the practical difficulties in adhering to the current COD procedure².

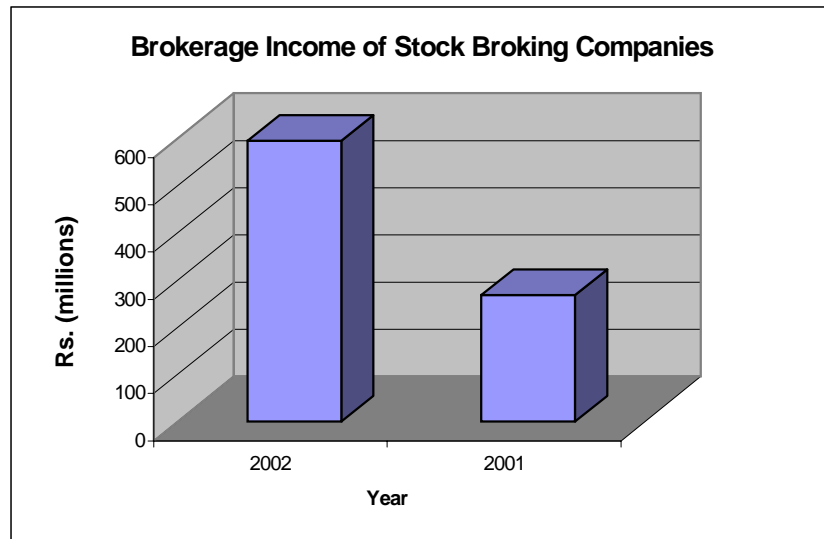
¹ A minimum net capital requirement is defined as shareholders' funds adjusted by all unsecured amounts.

² The Procedure was laid down before stock brokers commenced using automated systems

Performance of the Stock Broking Companies

The overall brokerage income earned by Broking Companies during the year 2002 was Rs. 595 million (approx.), an increase of Rs. 327 million (approx.) compared to the year 2001. The main reason for the increased brokerage income was due to the enhanced investor confidence in the market, which, in turn, raised the turnover and market prices during the year. This was evident with the All Share Price Index recording a five year high on 26th September 2002 of 860.3 points and the Milanka Price Index reaching the highest point since its inception in January 1999 on the same day of 1,463.9 points.

The following graph depicts the total income of Stock Broking Companies in the years 2001 and 2002:

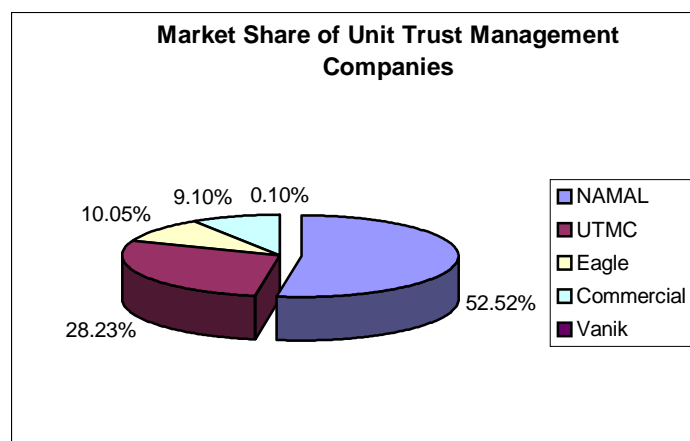


It is evident from the above graph, that during the year 2002 the Brokerage Income increased substantially in line with the bullish market trend.

Supervision of Unit Trust Management Companies

There were thirteen Unit Trust Funds managed by five Management Companies as at 31st December 2002.

The market share of each Unit Trust Management Company as at 31st December 2002 is depicted in the following chart:



Structure of the Management Companies

Names of the five Management Companies and the thirteen Unit Trust Funds are listed below:

Management Company	Managed Unit Trusts
National Asset Management Company Ltd.	National Equity Fund Namal Growth Fund Namal Income Fund Namal Optima Fund
Unit Trust Management Company (Pvt.) Ltd.	Ceybank Unit Trust Ceybank Century Growth Fund
Eagle NDB Fund Management Company Ltd.	Pyramid Unit Trust Eagle Income Fund Eagle Growth Fund Eagle Gilt-edged Fund
Commercial Fund Management Company (Pvt.) Ltd.	Comtrust Equity Fund
Vanik Asset Management Co.Ltd.	Vanik Index Fund Vanik Income Fund

The Supervision Division visited each Management Company once during the year under review. The inspections were carried out in accordance with the Audit Programme developed by the SEC in order to verify whether the investment parameters were maintained as set out in the Unit Trust Code and relevant Trust Deeds and whether the Management Companies were financially stable. A few discrepancies were noted such as applications being incomplete and cheque payments to unitholders being delayed for more than seven days for unit redemptions. Although the discrepancies were not considered material, the Management Companies were nevertheless informed thereof.

The SEC reviewed the monthly accounts and returns submitted to the Commission in respect of the thirteen Unit Trust Funds. In addition to the above, the SEC approved advertising materials, interim reports and annual financial statements. The documents submitted and information sent to the SEC were found to be satisfactory.

Performance of the Unit Trusts

The Unit Trust Industry recorded a negative growth of 3.22 per cent in terms of Unit holders and 1.45 per cent in units created, while the fund value recorded a positive growth of 20.11 per cent when compared to the previous year.

Details of the funds with regard to number of units, number of unit holders and value are as follows:

	General Purpose Funds	Growth Funds	Index Fund	Income Funds	Gilt-edged Funds	Total
No. of Units - 2001	328,802,894	27,804,556	165,510	17,091,663	91,497,407	465,362,030
- 2002	322,140,150	25,958,346	237,609	18,486,361	91,800,626	458,623,047
Unit Holders- 2001	23,257	1,373	54	666	743	26,093
- 2002	22,517	1,279	49	661	746	25,252
Fund Value - 2001 in Rs.	2,270,751	264,557	2,018	187,325	951,036	3,675,687
-2002	2,829,534	323,259	3,625	203,834	1,054,699	4,414,951

At the end of year 2002, thirteen unit trust funds recorded 459 million units in circulation compared to 465 million at the end of year 2001. The number of unit holders had decreased from 26,093 as at 31st December 2001 to 25,252 as at 31st December 2002. The overall Net Asset Value of funds increased by Rs. 0.07 billion (approx.) from Rs. 4.3 billion to Rs. 4.4 billion compared to the previous year. Approximately 83% of the Unit Trust Funds (excluding Income Funds) were invested in the equity market. Income Funds invested on an average more than 47% of their funds in Treasury Bills. Due to the improved market conditions, the Net Asset value of the funds showed an increase during the year under review.

**THE OVERALL POSITION OF UNIT TRUST FUNDS AS AT 31ST DECEMBER 2002 AND
31ST DECEMBER 2001**

	31/12/02	31/12/01	Change %
Net Asset Value (NAV) (Rs. Mn.)	4,415	3,676	20.1
No. of Unit Holders	25,252	26,093	(3.22)
No. of Units Issued ('000)	458,623	465,362	(1.45)
Investment in Equity (Rs. Mn)	2,536	1,108	128.9
Investment in Treasury Bills (Rs. Mn)	1,330	1,097	21.2
Investment in other Instruments (Rs. Mn) ¹	549	1,471	(62.7)

¹ E.g. Commercial Papers, Promissory Notes and Debentures

Public Relations and Market Development

CORE FUNCTIONS

- ▶ Handle international relations.
- ▶ Handle publications.
- ▶ Develop and conduct training programmes on the Capital Market, Securities Law and related subjects.
- ▶ Conduct training programmes for SEC Staff.
- ▶ Coordinate the development of the SEC library.

KEY ACTIVITIES

International Relations

- **International Organization of Securities Commissions (IOSCO)**

The SEC participated in the Annual Conference held in Istanbul, Turkey and made a bid to host the IOSCO Annual Conference in Sri Lanka in the year 2005. Sri Lanka won the bid having competed with Spain. The Asia Pacific Regional Committee (APRC) meeting which was scheduled to be held in Sri Lanka in October 2002, will be held in January 2003. The SEC participated in the APRC meetings held in Malaysia and Indonesia and the Emerging Markets Committee meeting in Malaysia.

- **Orientation Programme at the Securities Commission Malaysia**

The SEC arranged a one week Orientation programme through the Securities Commission of Malaysia for four members of the Stock Brokers' Association; Senior Manager, Surveillance, Colombo Stock Exchange and two officials of the SEC. The programme was held from 29th July to 2nd August 2002. The SEC funded the participants of the Stock Brokers' Association and the official of the CSE.

- **Orientation Programme for members of the Unit Trust Association at the Thai SEC**

The SEC coordinated an orientation programme for the Unit Trust Association of Sri Lanka with the Securities and Exchange Commission of Thailand on the Mutual Fund Industry in Thailand. The programme was held from 25th to 28th November 2002. The SEC part funded the participants of the Association. Following are some of the recommendations made by the participants:

- All asset management related business to be brought under one regulatory body to ensure a uniform approach to regulate relevant businesses.
- Permit Unit Trust to invest abroad while specifying the maximum limit the industry can invest.
- Unit Trust should receive due recognition as a vehicle to attract savings into capital market.

- **Orientation Programme on Internet Trading at the Korean Stock Exchange**

The SEC arranged an orientation programme on Internet Trading with the Stock Exchange of Korea for six members of the Stock Brokers' Association and two officials from the Colombo Stock Exchange and the SEC.

The programme was held from 25 - 28 November 2002. The SEC part funded the Stock Brokers' Association. The participants made the following recommendations:

- o The Colombo Stock Exchange to provide on line service to brokers and investors at a reasonable price.
- o The CSE to develop a more advanced and informative Internet disclosure system that investors can easy access to.
- o Request Broking Companies to enhance their IT infrastructure.

- **Regional Training Programme on Capital Market of Sri Lanka**

The SEC and the Insurance Board of Sri Lanka in collaboration with the Ministry of Foreign Affairs organized a Regional Training Programme on "Capital Market of Sri Lanka" for the participants of South & East Asian Countries.

The programme was held from 20th February to 13th March 2002. Eleven participants from Maldives, Myanmar, Bhutan, Nepal, Laos, Cambodia and Iran participated in the programme. Two Sri Lankans were also included in the programme.

- **Technical assistance from ADB**

A team of ADB consultants is provided technical assistance in the following reform areas:

- o Establishment of an Integrated Financial Regulator
- o Formulation of a Code of Best Practices for Securities Market Participants
- o Demutualization of the Colombo Stock Exchange

Publications

The following were published during the period under review:

- Annual Report 2001 of the Securities and Exchange Commission of Sri Lanka
- Third edition of the Sinhala publication on the "Securities market of Sri Lanka" by Dr. Lalith Samarakoon
- Two issues in the "Document Reproduction Series".

Training

- **National Institute of Education (NIE)**

The SEC, in association with the NIE, organized a comprehensive training programme in the Sinhala medium to educate regional master teachers, resource teachers and additional Directors of Education on the subject of Capital Markets and current developments. The programme was held at the NIE auditorium, Maharagama, with a field visit to the Colombo Stock Exchange. This three-day residential programme gave the participants from the provinces an opportunity to update their knowledge on the Capital Market.

The SEC was instrumental in introducing the subject of capital market to the Advanced Level curriculum in the early 1990's. Annually about 60,000 Advanced Level Commerce students offer the subject at the examination. Currently the subject of capital Markets has also been included in the Ordinary Level Curriculum, exposing the subject to over 500,000 students.

Other seminars and programmes

• **Government's 100 Day Action Programme**

The SEC organized a series of public awareness campaigns to encourage women to invest in the Colombo Stock Market under the Government's 100 day action programme.

The Colombo Stock Exchange and Stock Brokers participated, thus facilitating the opening of security trading accounts. A total of 1,142 participants attended the seminars and 320 new security trading accounts were opened on the spot. Seminars were conducted for the following associations:

- Sri Lanka Association of Personal Secretaries.
- Sri Lanka House Wives' Association - Kandy Branch
- Sri Lanka House Wives' Association - Galle Branch
- Sri Lanka House Wives' Association - Matale Branch
- Sri Lanka House Wives' Association - Kurunegala Branch
- Doctors Wives' Association
- Women Lawyers' Association
- Association of Corporate Lawyers

• **SEC Consultation on the Role of Auditors**

The Division organized a full day consultation on the "Role of Auditors" on 9 May 2002. A total of one hundred and thirty participants attended the consultation. The participants included auditors nominated by the Institute of Chartered Accountants, participants from listed Companies, Insurance Companies, Law Firms, Stock Brokers and Unit Trust Companies. At the consultation it was proposed to study the regulatory regime governing the auditors and identify whether there is a need for further regulations in order to protect investors of the capital market. A committee was set up to study the role of auditors.

• **SEC Consultation on Capital Market Reforms**

A full day consultation on "Capital Market Reforms" was held on 12 July 2002. A total of 91 participants from the Colombo Stock Exchange, Stock Brokers, listed companies, Unit Trust Management Companies, Custodial Banks and Law Firms attended the consultation. The following areas were covered at the consultation:

- Building investor confidence - The way forward
- The changing role of market intermediaries
- Regulator as a facilitator of market development
- Corporate Governance in Listed Companies

• **Discussion on the proposed Unit Trust Code**

The Division conducted a half a day discussion on the "Proposed Unit Trust Code" on 13 August 2002. A total of sixty participants from the Unit Trust Management Companies, Banks, and Law Firms attended the discussion.

• **Public Lectures**

Public lectures on "Insider Dealing" and "Money Laundering" were delivered by Prof. Barry Rider, Director of the Institute of Advanced Legal Studies of the University of London on 21 February 2002. Over 140 participants attended the lectures.

The SEC conducted and participated in the following seminars:

- o Programme on Securities Market Regulation for the Sampath Bank Staff.
- o Presentation on Securities Market Regulation for the Peoples' Bank Regional Managers.
- o Stock Market promotion programme at the Colombo Medical Faculty.
- o Programme on Investing in the Stock Market and the Role of SEC for the Businessman's Club, Kurunegala.
- o Programme on Capital Market for students of the Bibile Maha Vidyalaya.
- o Programme on Capital Market for Master Teachers of Gampaha District.

• **Distribution of books in Vavunia**

Officials of the SEC visited the Divisional Education Office of the Education Department in Vavunia to handover a consignment of books on the "Securities Market of Sri Lanka" authored by Dr. Lalith Samarakoon (in Tamil) to be distributed free of charge to Advanced Level students and school libraries in the North East Province. Discussions were held with the education officials to conduct a three-day residential training programme in Tamil on the "Capital Market of Sri Lanka" for North East Teachers at the NIE, Maharagama in January 2003.

• **"Yuga Dekma" Industrial Exhibition in Trincomalee**

The SEC took part in the above exhibition which was organized by the Ministry of Industries. This was held from 16 - 20 August 2002 at Trincomalee. The Colombo Stock Exchange and the Unit Trust Association also participated.

• **Training Programmes for the SEC Staff**

Several in-house training programmes were conducted for the staff on technical issues and subjects of general interest on every Thursday afternoon. Among the subjects covered were:

- o Banking and Financial reforms in Sri Lanka
- o Risk Management
- o Corporate Governance
- o Preliminary findings of the Census 2001 and the use of Census data in Development Planning
- o New Inflation Index
- o Unit Trust Industry in Sri Lanka

A residential outdoor training programme was held for the SEC Staff in September. The programme focused on teamwork and leadership.

• **Library Development**

The SEC is continued its library development programme by adding more books to its collection. Details of books are now available in a computerized database.

Unit on Policy Development

CORE FUNCTIONS

- ▶ Study legislative changes required to facilitate market development;
- ▶ Undertake comparative surveys in order to ascertain shortcomings in existing laws and regulations;
- ▶ Compile surveys to clarify the existing situation with regard to various concepts and procedures;
- ▶ Provide information backstopping services to other Divisions with regard to regional and international trends and developments.

KEY ACTIVITIES

Research

The Unit undertook a major review of all Commercial Laws for an IMF sponsored project on financial reforms and assessed the shortcomings in approximately 30 laws relating to the financial sector. Problem areas, current shortcomings, impediments and prospective amendments to the Acts under consideration were identified. A research paper was presented at the Financial Sector Reform Conference.

Consultation on the Role of Auditors

The SEC held a Consultation on “The Role of Auditors” in March 2002 in the wake of various corporate frauds that unfolded in the United States. At the Consultation it was proposed that a detailed examination be made of the regulatory regime governing Auditors in order to identify if there is a need for further regulations in order to protect investors. As a follow up to this Consultation, the SEC set up a Committee to study “The Role of Auditors”.

During the period under review the Unit studied and compiled a research report on the various laws governing Auditors in Sri Lanka.

The Unit also prepared a paper on Audit Committees based on information from various countries.

The Committee recommended that a Code be drafted and certain provisions from the Sarbanes – Oxley be included. Based on the meetings of the Committee the Unit is in the process of finalizing the report and organizing a public seminar.

Consultation on Capital Market Reforms

The SEC held a Consultation on Capital Market Reforms in July 2002. The Central Bank set up an Insurance and Securities Reforms Task Force under the Chairmanship of the Director General of the SEC. The Task Force completed its major task of addressing the relevant issues and concrete action has been taken to resolve most of the issues and identify the course of action to be pursued to resolve the rest of the issues. The findings were presented at the Financial Sector Reforms Committee meeting held in December 2002 at the Central Bank.

The proposals were considered in relation to the underlying objectives such as: injecting liquidity into the market; attracting investors and investor protection; more effective regulations; maximising returns from investments; greater disclosure; achieving administrative efficiency and better governance within listed companies and insurance companies.

Unit on Information Technology and Publications

CORE FUNCTIONS

- ▶ Develop, maintain and upgrade in-house software systems.
- ▶ Maintain and upgrade the SEC web-site.
- ▶ Format and finalize all in-house publications.
- ▶ Maintain and update the library system.
- ▶ Conduct IT related training programmes for staff members.
- ▶ Handle advertisements and press releases.

KEY ACTIVITIES

Publications

The Unit coordinated the preparation of the Securities and Exchange Commission Annual Report 2002 as well as the other reports.

Maintenance of the SEC web-site

The Unit updated the website by routine changes and upgrades in addition to several changes being done in order to make the website more informative and user-friendly.

Maintenance of the Software System

The Unit coordinated the upgrading of the computer infrastructure. Additionally the Unit ensured that all systems were protected against common computer viruses.

Finance and Administration Division

CORE FUNCTIONS

- ▶ Financial control and budgeting including preparation of monthly, quarterly, and annual accounts.
- ▶ Manage the Cess Fund, Compensation Fund and Settlement Guarantee Fund.
- ▶ Deal with personnel management including recruitment, promotions, staff welfare, compensation and benefits.
- ▶ Supervise general maintenance and upkeep of the Secretariat.
- ▶ Handle purchasing and insurance.
- ▶ Handle publication of reports and submission of the Annual Report to Parliament.

KEY ACTIVITIES

Staffing

From its inception SEC has placed emphasis on recruiting qualified personnel with recognized experience. The Commission has constantly provided appropriate training-both local and foreign-to adequately gear them to meet the challenges of developing and regulating the Securities Market.

During the year under review, 5 Executives and 2 non-Executive staff members were recruited. Two members of the staff resigned, one member retired upon reaching the age of 55 and one member left the Secretariat upon the expiration of his contract. In addition, the services of a member of the staff was also terminated after conducting a disciplinary inquiry.

The “Managers” of the Secretariat were re-designated as “Directors” during the year under review.

As at 31.12.2002, the SEC had 49 staff members as against an approved cadre of 55. Out of the 49 members of staff 18 are males and 31 are females.

The approved cadre and the Human Resource strength of the Commission as at 31.12.2002 are depicted below:

Post	Approved Cadre	In employment
Director General	01	01
Directors	08	06
Executives	22	19
Staff	17	16
Office Aides	07	07
Total	55	49

Training

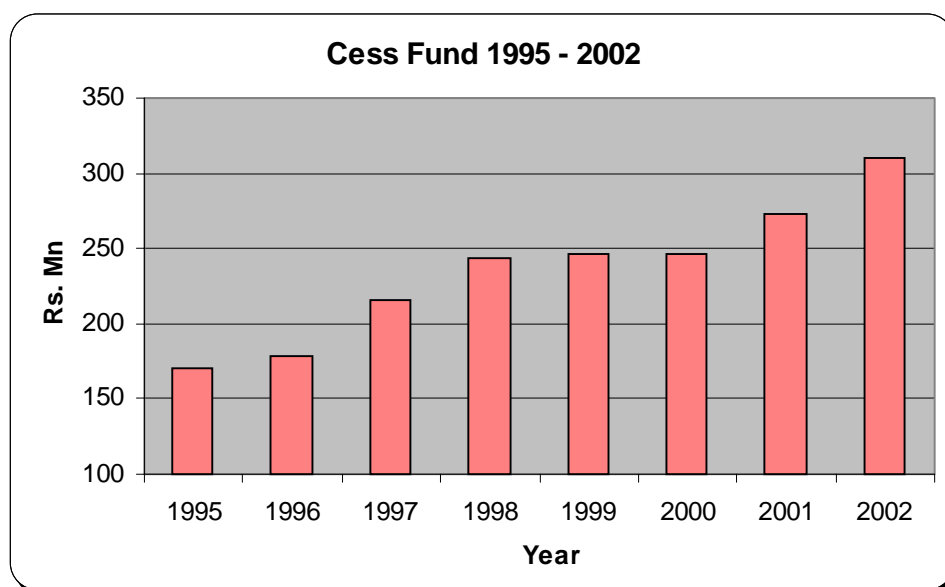
Training provided during the year covered several areas such as capital market development, corporate governance, risk management, Sri Lanka accounting standards, information technology developments, secretarial skills, recruitment techniques and laws applicable to the termination of employment. Staff attended 51 training courses and seminars during the year under review. Attempts were made to provide training to the staff at every level:

Post	Local Training Courses	Foreign Training Courses
Director General	Nil	Nil
Directors	04	11
Executives	12	10
Staff	12	01
Office Aide	01	Nil
Total	29	22

The Cess Fund

The SEC, pursuant an administrative arrangement with the Colombo Stock Exchange, levies a Cess on share trading transactions of the Colombo Stock Exchange in order to enable the Commission to reduce its dependence on the Treasury for funds to finance its market, regulatory and development functions and administrative expenses. The Ministry has granted approval to the SEC to levy such Cess. The rate of Cess charged by the SEC is 0.1% of each transaction. The balance lying to the credit of the Fund as at 31.12.2002 amounted to Rs. 310 million.

The growth of the fund during the period 1995 – 2002 is depicted below:



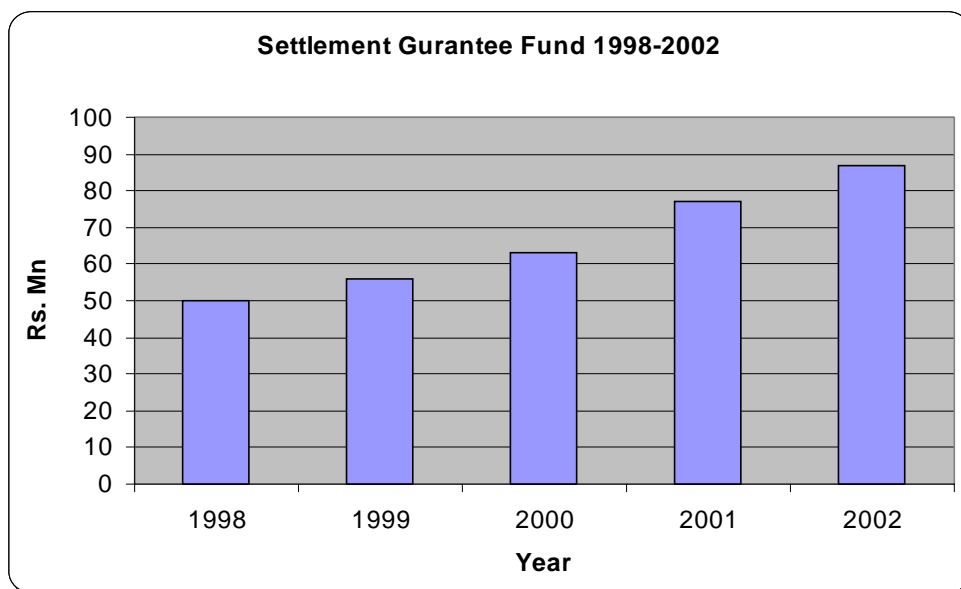
The Settlement Guarantee Fund (SGF)

- The SGF was launched on 22 May 1998. The Fund was established for the purpose of guaranteeing the settlement of trades between participants of the Central Depository System of the Colombo Stock Exchange. The operation of the SGF is as follows:
- The settlement cycle presently followed in CSE is of a two-tiered nature.

Ownership of shares traded is transferred no sooner a trade is executed. The buyer is required to pay on T+5 i.e. the 5 day following the day of trading and the seller is settled on T+6 i.e. the 6 day following the trade. This relatively long interval between transfer of ownership and receipt of proceeds which gave rise to an unsecured settlement risk necessitated the establishment of SGF.

- The Trustees of the Fund hold office ex-officio and comprise the Chairman of the SEC, the Chairman of the CSE, the Deputy Secretary to the Treasury, the Director General of the SEC and the Director General of the CSE.
- The Government of Sri Lanka has contributed a sum of Rs.50 million to the said Fund. This money has been invested in Government securities in terms of the Trust Deed. SGF can also receive donations, gifts and endowments as replenishments. The broker/custodian banks are presently not required to contribute to the Fund.

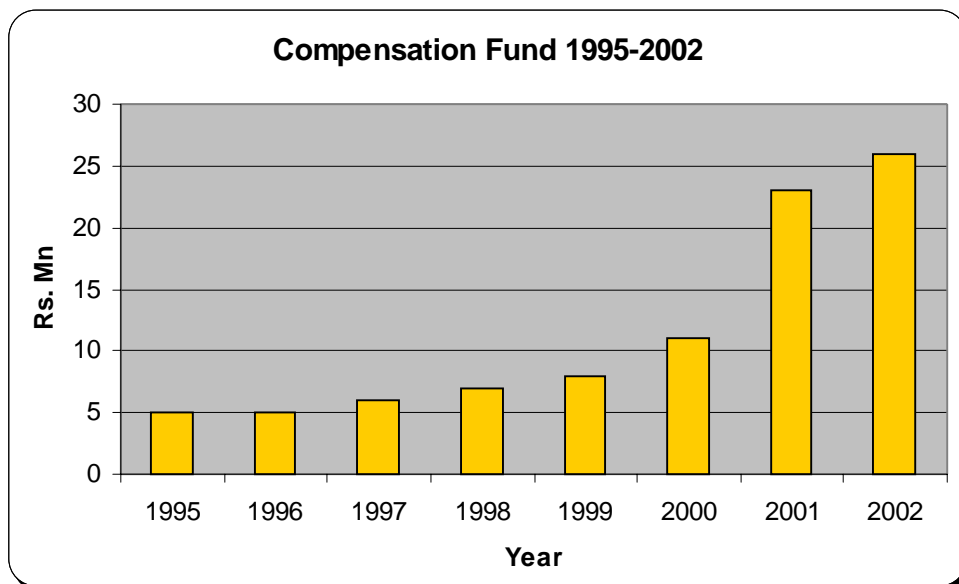
The balance lying to the credit of the fund as at 31.12.2002 amounted to Rs. 87 million. The growth of the Fund between 1998 and 2002 is depicted in the following graph:



The Compensation Fund

- The Compensation Fund came into operation along with the establishment of the SEC in 1987. The Securities & Exchange Commission Act No. 36 of 1987 as amended states as follows:
- A Compensation Fund shall be established for the purpose of granting compensation to any investor who suffers pecuniary loss resulting from the failure of a licensed stock broker or licensed stock dealer to meet his contractual obligations.
- The Compensation Fund shall consist of -
 - such sums of money as may be voted upon by Parliament for the purpose of the Fund;
 - such sums of money as may be credited to the Fund under Section 51A;
- “The Minister shall appoint from among the members of the Commission three members who shall comprise the Compensation Committee. The Committee shall be responsible for assessing and awarding compensation in respect of any application made and the decision of such Committee on any such assessment or award shall be final and conclusive”.
- The Act also provides for the procedure for applying for compensation. According to the Act, the Committee may, after examination of the documents and other evidence produced in support of the claim by an applicant, or in any case where an inquiry was held on the conclusion of such inquiry, allow or disallow such claim for compensation. Uptodate there have been no claims.

The balance lying to the credit of the fund as at 31.12.2002 amounted to Rs. 26 million. The growth of the Fund is depicted below:



Calendar of Events for 2002



Presentations for the SEC staff on

- Banking and Financial Law Reforms in Sri Lanka
- New SEC Rules
- Role of the Bank of International Settlements



Public lectures on “Insider Dealing” and “Money Laundering” by Professor Barry Rider Director of Advanced Legal Studies, University of London.

Regional Training Programme on the Capital Market of Sri Lanka for participants from South and East Asian countries.

Presentation on “Securities Market Regulation” for the People’s Bank Regional Managers.

Government’s 100 Day Action Programme - seminars conducted for the following Associations:

- Sri Lanka Association of Personal Secretaries
- Sri Lanka House Wives’ Association
- Sri Lanka House Wives’ Association - Kandy Branch



Government’s 100 Day Action Programme - seminars conducted for the following Associations:

- Sri Lanka House Wives’ Association - Galle Branch
- Sri Lanka House Wives’ Association - Matale Branch
- Sri Lanka House Wives’ Association - Kurunegala Branch
- Doctors Wives’ Association



Government’s 100 Day Action Programme - seminars conducted for the following Associations:

- Women Lawyers’ Association
- Association of Corporate Lawyers

A three-day residential programme for Women Master Teachers and Resource Teachers at the National Institute of Education, Maharagama.



MAY

Consultation on the “Role of Auditors” for participants nominated by the Institute of Chartered Accountants and participants from listed Companies, Insurance Companies, Law Firms, Stock Brokers and Unit Trust Companies.

Stock Market Promotion Programme for the members of the Medical profession at the Colombo Medical Faculty.



JULY

Consultation on “Capital Market Reforms” for participants of the Colombo Stock Exchange, Stock Brokers, listed Companies, Unit Trust Management Companies, Custodial Banks and Law Firms.

Training session on “Capital Market” for students of the Bible Maha Vidyalaya.



AUGUST

Consultation on the “Proposed Unit Trust Code” for the participants of 5 Unit Trust companies and Trustee Banks.

Presentation on the Unit Trust Industry in Sri Lanka



SEPTEMBER

Presentation on the “Demutualization of the Stock Exchange” by the ADB consultants for the CEO’s of Stock Broking companies and officials of the Colombo Stock Exchange.

Seminar on the “Securities Market of Sri Lanka and the Role of the SEC” for the Master Teachers of Gampaha District.

Two day residential training programme for the SEC staff.



OCTOBER

Visit to the Education Directors’ office in Vavunia to handover a consignment of books on the “Securities Market of Sri Lanka” (in Tamil).



NOVEMBER

Presentation on the proposed Financial Service Authority (FSA) by the ADB Consultants.

Seminar on “Capital Market of Sri Lanka” for Management Faculty students of the Rajarata University, Mihinthale.



DECEMBER

Presentation on the “Demutualization of the Stock Exchange” by the ADB Consultants with the participation of senior officials of the Colombo Stock Exchange and CEO’s of Stock Broking companies.

