



Securities and Exchange Commission of Sri Lanka

"Weaving pathways to a secure Financial Market"

Annual Report
2006

Our Vision

To become the benchmark regulator in Asia for effective,
efficient and proactive securities market regulation.

Our Mission

To promote,
develop and maintain a securities market that is fair,
efficient, orderly and transparent.

The Securities and Exchange Commission of Sri Lanka (SEC) was established by the Securities Council Act No. 36 of 1987 to regulate the Securities Market in Sri Lanka, grant licenses to Stock Exchanges, Stock Brokers and Stock Dealers who engage in the business of trading in securities. Subsequently, the Act was amended by the Securities Council (Amendment) Act No. 26 of 1991 vesting the SEC with the power to license and regulate Unit Trusts. The development and expansion in the Capital Market resulted in an increase of Market Intermediaries performing securities related functions, thus leading to gaps in the regulatory framework. Taking this into consideration Underwriters, Margin Providers Investment Managers, Credit Rating Agencies and Clearing/Depository Houses were brought under the purview of the SEC with Securities and Exchange Commission (Amendment) Act No. 18 of 2003.

Since its creation, the SEC's ultimate responsibility has been to protect investors, and to maintain a fair, efficient and orderly market. Apart from discharging its regulatory functions, it is also obliged to encourage and promote the development of the Securities Market. In the year under review the Commission in order to fulfil its responsibilities pertaining to effective market supervision, development, regulation and enforcement embarked on several strategic initiatives.

The activities and accomplishments highlighted in this Annual Report for the year 2006 demonstrate our commitment to developing the Capital Market of Sri Lanka by strengthening regulation and enforcement and thereby promoting investor confidence.

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Members of the Commission



From Left to right: Mr. Yohan Perera, Mr. D. K. Hettiarachchi, Dr. Gamini Wickramasinghe (Chairman), Mr. C.P.E. Gunasingam, Mrs. Siromi Wickramasinghe, Dr. Raneer Jayamaha.

Absent: Mr. Sumith Abeysinghe, Mr. Graetian Gunawardhana, Mr. Ravi Abeysuriya.

Dr. Gamini Wickramasinghe (Chairman)

Dr. Wickramasinghe graduated with a MSc. in Systems Analysis from the University of Aston, Birmingham, U.K. With over a decade of extensive senior level experience obtained in the United Kingdom and Belgium, he returned to Sri Lanka in 1983 and founded the Informatics Group of Companies. Considered a pioneering 'Information Technology' company, today Informatics consists of a multitude of companies complementing the national education goals through the introduction of locally based quality British tertiary education in Sri Lanka and creating employment opportunities nationwide as one of the largest software development houses in the country.

Dr. Wickramasinghe obtained his Doctorate in Business Administration from Manchester Metropolitan University, UK and is a Fellow Member of the British Computer Society and the Chartered Management Institute of U.K. Apart from being the Chairman of the Securities and Exchange Commission of Sri Lanka, presently he holds the chairmanship of the Insurance Board of Sri Lanka and the Bank of Ceylon.

Mr. D.K. Hettiarachchi

Mr. D.K. Hettiarachchi is an Attorney-at-Law by profession. He is a Law Graduate (L.LB) of the University of Colombo.

He joined the department of the Registrar of Companies in 1986 as an Assistant Registrar and was promoted to the position of Registrar of Companies in 1997. He has been appointed as the Registrar General of companies under the new Companies Act.

He is also an ex-officio member of the Sri Lanka Accounting and Auditing Standards Monitoring Board.

Dr. Raneer Jayamaha

Dr. Raneer Jayamaha currently holds the post of Deputy Governor, Central Bank of Sri Lanka. As the Deputy Governor in charge of the Financial System Stability, she chairs the Financial Stability Committee of the Bank. She is also the Chairperson of Credit Information Bureau of Sri Lanka and the National Payments Council. She is a Member of the Bank's Monetary Policy Committee, Insurance Board of Sri Lanka, Securities and Exchange Commission of Sri Lanka and the Economic Council. Dr. Jayamaha held the posts of (i) Special Advisor (Economics), Economics & Legal Advisory Services Division, Commonwealth Secretariat, London, U.K.; (ii) Advisor/Chief Executive, Financial Sector Reform Committee, Ministry of Finance – Colombo; (iii) Secretary, Presidential Commission on Finance & Banking; and (iv) Director, Banking Development Department, Central Bank of Sri Lanka.

She received her Ph.D in Monetary Economics from University of Bradford, U.K.; M.Sc in Economics from University of Stirling, U.K. and BA (Hons.) from University of Peradeniya, Sri Lanka.

Mr. Sumith Abeyasinghe

Mr. Sumith Abeyasinghe holds a Bachelor of Arts (Hons.) Degree in Geography (Sri Lanka) and a Masters Degree in Economics (University of New England, Australia).

Mr. Abeyasinghe functions as Deputy Secretary to the Treasury. He previously held senior positions in the Ministry of Finance and Planning such as Director General of National Budget and Director of Fiscal Policy and Economic Affairs. He is also an ex-officio Director of Bank of Ceylon.

Mr. Yohan Perera

Mr. Yohan Perera is a Partner at KPMG Ford Rhodes, Thornton & Company since April 1990.

Mr. Perera is the President of the Institute of Chartered Accountants of Sri Lanka for the years 2006 and 2007. He is also a Director of the Confederation of Asian and Pacific Accountants (CAPA), a regional accountancy organisation affiliated to the International Federation of Accountants (IFAC).

Mr. Perera is an ex-officio member of the Governing Council of the Post Graduate Institute of Management of Sri Jayawardenapura (PIM) and the National Institute of Business Management (NIBM). He is also a Member of the Monetary Policy Consultative Committee of the Central Bank of Sri Lanka and the Inter Regulatory Institutional Council.

He is a Fellow Member of the Institute of Chartered Accountants of Sri Lanka (FCA) and a Fellow Member of the Chartered Institute of Management Accountants, U.K. (FCMA).

Mr. C.P.E. Gunasingam

Mr. C.P.E. Gunasingam holds a Bachelor of Science degree from the University of Madras and a Bachelor of Laws degree from the University of Colombo. He was admitted

to the Bar as an Advocate in 1972. He's a Fellow Member of the Sri Lanka Institute of Taxation and has served as its President for 4 years. He has served as a Visiting Lecturer in Taxation at the Sri Lanka Institute of Taxation and the Institute of Chartered Accountants of Sri Lanka. He has served as an assessor of Inland Revenue from 1962 to 1973 and counts 33 years of service as a tax practitioner. He has addressed seminars and contributed articles to newspapers and journals on tax related subjects. Mr. Gunasingam served as a Board Member of Peoples Bank. Presently he serves as a Board Member of the Insurance Board of Sri Lanka and the National Council for Economic Development – Taxation Cluster.

Mr. Graetian Gunawardhana

Mr. Graetian Gunawardhana was educated at Thurstan College and studied up to Advanced Level and joined the Royal Ceylon Air Force as an Aircraft Engineering Technician for 02 years and thereafter served in the Police Department for 12 years.

He started his own business as the founder Chairman of Hands International (pvt) Ltd, which is an export oriented company with a staff of 3000 workers. He was elected the entrepreneur of the year in 1999/2000. Mr. Gunawardhana was the recipient of the Gold Award for exports for the extra large category for many years.

He also served as the Chairman of the Exporters Association from 2003-2005. He was also the Chairman of the Sri Lanka Taiwan Friendship Association for five years. Mr. Graetian Gunawardhana was a Director of the America Chamber of Commerce for 2 years.

Presently he's the Lions Governor for District 306 B2 and was adjudged the best Governor in the world at the Boston Academy Awards Function. He's also a new Board Member of the Lions Club International.

Mrs. Siromi Wickramasinghe

Mrs. Siromi Wickramasinghe is a senior banker with over 25 years of experience in the industry and presently functions as the General Manager/CEO at Lankaputhra Development Bank Ltd. She has held many positions in the spheres of Credit Development and Investment

Members of the Commission Contd...

Management, Procurement and Expense Control and Corporate Relationship Development, Regulation and Corporate Governance and Administration. She has extensive exposure to global industry best practices having taken part in and contributed to many training and development programmes at some of the worlds' leading financial centers.

Mrs. Wickramasinghe is also an Attorney-at-Law, Notary Public and Commissioner for Oaths and a Fellow of the Chartered Management Institute, U.K. where she is the Treasurer of the Executive Council of the Sri Lanka branch.

Mr. Ravi Abeyseriya

Mr. Abeyseriya is a Fellow Member of the Chartered Institute of Management Accountants, U.K., and has an MBA from Monash University, Melbourne, Australia. He is one of the very first CFA (Chartered Financial Analyst) Charter holders in Sri Lanka.

As Head of Corporate Finance at JP Morgan/Jardine Fleming he was responsible in carrying out international equity placements and corporate restructuring assignments. In 1999 he pioneered the establishment of Sri Lanka's first credit rating agency, Fitch Rating Lanka Limited and worked in the capacity of Managing Director and Chief Executive Officer.

As a Member of Sri Lanka's Prime Ministerial task force he was responsible for recommending financial sector reforms in Sri Lanka.

His work experience also includes senior roles in the private equity investment industry, and consulting for the World Bank and the Government of Sri Lanka.

At present, Mr. Ravi Abeyseriya is the Managing Director of Amba Research and heads a specialized provider of investment research and analysis support services.

Senior Management



Seated (from left)

Himani Kotagama (Assistant Director, Supervision)
Marina Fernando (Director, Legal and Enforcement)
Ianthie Jayaratne (Director, Finance and Administration)
Surana Fernando (Director, Corporate Affairs)

Standing (from left)

Malik Cader (Director, External Relations and Market Development)
Namal Kamalgoda (Director, Capital Market Development Asset Management)
Toshihisa Iida (Consultant)
Dhammika Perera (Director, Investigations)
Channa de Silva (Director General)
Chandu Epitawala (Director, Surveillance and Research)
P M C Thilakerathne (Director, Financial Services Academy)
Vasula Premawardhana (Director, Media and Communication)
Vajira Wijegunawardene (Director, Capital Market Development)

Staff



Front Row (from left):

W Ariyaratne, Avanthi Weerasinghe, Krishanthi Muthuthanthrige, Kaushalya Kumarage, Chamila Vithana, Shalini Perera, Lakshmi Wickramanayake, Madugayanie Balapitiya, Dayanthi Panabokke, Ruwanganie Gooneratne, Julie AllegaKoen, Manjula Chandraratne

Middle Row (from left):

P W L Piyatissa, Kishan Abeygunawardana, Dhanesha Rajapura, Prabashini Samarakoon, Sharmila Panditharatne, Carmen de Silva, Ranmini Jayathilake, Ashoka K Dayarathne, Sheena Goonarathne, Kumari Siriwardena, Hasini Amaratunga, Dinesha Perera, Shalini Samarakkody, Rupika Bandara, P W Anusha Nishanthi, Christobel Silva, Chandran Nagendran

Last Row (from left):

Anura Perera, Suneth Perera, Anslam Dias, R K W Sunimal, S D Dharmasiri, D M G Priyantha, Pathum Niroshana, Sugath Alwis, Nimal Kumarasinghe, M Jayasekera

Absent:

A G I Priyanganie, Mekala Jayapala, Nishoka Jayathunga, Sajeewani Bakmedaniya, Thushara Abeyratne

Reviews



Chairman's Review



The new Commission Members appointed by the new government took office in March 2006. The first task of the Commissioners was to take full stock of the status quo of the SEC Secretariat, in terms of what has been accomplished, policy issues, and the challenges ahead. This in turn formed the basis for new policy directions at the SEC. As one of my first steps in this regard, I called upon Ernst & Young Malaysia to commence a study on the Sri Lankan Capital Market and design a Capital Market Development Master Plan modeled after the successful Malaysian Plan. Their report & recommendations were submitted to the SEC in August 2006.

After having studied and identified the issues & challenges for the Sri Lankan Capital Market vis-à-vis other regional markets such as India, Malaysia and Thailand, we recognised the need and the benefit for the country to accelerate the development of the Capital Market in Sri Lanka. This led the SEC to take a more active role in the development of the Capital Market without neglecting in any way the core roles of monitoring and regulating the Capital Market activities.

We have also embarked on increasing the staff strength of the Secretariat with the inclusion of two new directorates of Financial Services Academy and the Capital Market Development with a dedicated Project Office. Areas where staff strength was lacking was addressed and the decision to relocate the SEC was made. Further, the salary structure of the staff of the Secretariat was revised to reflect the industry standards with a view to attracting and retaining competent professionals to the SEC.

During the year under review we hosted the first South Asian Securities Regulators Forum in Colombo where a Memorandum of Understanding was signed for greater cooperation among South Asian regulators. This helped us renew our friendship with fellow regulators from the region and forge new ties. Globalisation and the increase in capital movements has raised concerns among the international community to establish cooperation of worldwide regulators to combat money laundering activity by organised criminals and terror groups.

In most developed countries, Capital Markets play a pivotal role in efficient mobilisation of savings and channelling them to the most productive areas of an economy. In fact, in most developed and fast developing countries, the funds raised through Capital Markets exceed that of the Banking sector by 2 to 3 times. The traditional banks in those countries derive much of their income from Capital Market activity such as Investment Banking, Advisory Services, Asset Management etc. In Sri Lanka, the traditional intermediation process by banks is inefficient which is reflected in high cost of intermediation. It is for this reason we are keen to accelerate this disintermediation process in Sri Lanka so that more and more business houses can access lower cost funds through the Capital Market while allowing the saver to reap a higher return for savings. SEC's goal is to make the Capital Market become the conduit to raising 50% of funding requirements in the country (i.e. on par with the banking sector) from the current 29%.

During the year under review, SEC also initiated a new concept of distributing equity wealth of government and private sector business entities as well as government owned commercially viable real estate using a Mutual Fund structure. The Fund would be managed by a company fully owned by the government which is to eventually evolve into the investment arm of the government along the lines of Tamasek Holdings of Singapore. This concept was given the green light by the government in the Budget 2007 under the name National Wealth Corporation, later renamed "Jathika Isura" . This concept is expected to increase the market capitalisation and liquidity of the Colombo Stock Exchange while extending an opportunity to the rural populace of the country to own part of corporate Sri Lanka using an innovative financing scheme.

I wish to take this opportunity to thank the Commission Members and the staff for their high level of professionalism, enthusiasm and commitment which contributed to strengthening our regulatory framework, increasing enforcement and enhancing confidence in our Capital Market.

I look forward to another year of growth and achievement.



Gamini Wickramasinghe

Director General's Review



It gives great satisfaction to report that the Sri Lankan Stock Market was rated as one of the best performing markets in the region in 2006. The growth of 41.62% in the All Share Price Index together with the 51.43% growth in the Sensitive Milanka Price Index for the year reinforced the potential of the Sri Lankan Capital Market. These had resulted in the enhancement of the market capitalisation, which grew by 42.9% during the year to reach Rs. 834 Bn.

We realised that the Sri Lankan Capital Market could be taken to a much higher elevation if certain global best practices were adopted. It was a case of learning new developments from other countries, which had adopted such developmental activities. There was no reason to 'reinvent the wheel' as there were success stories from neighboring Asian countries, which had engaged in undertaking a developmental agenda.

After carefully studying global developments it was decided that countries such as Malaysia, Thailand, Singapore and India could offer much value addition and important lessons for the Sri Lankan Capital Market. Therefore we selected and invited the individuals and key personalities who were involved in drafting and executing the Capital Market Master Plan of Malaysia, to join the Sri Lankan SEC team to lay the foundation to develop a strategic plan for the Securities Market of our country to ensure that our Capital Market is well positioned to meet future challenges.

Together with the SEC team the Malaysian professionals obtained views of all the Capital Market stakeholders, in

developing the Capital Market Master Plan of Sri Lanka. This resulted in the creation of the ten-year Capital Market Master Plan aimed to provide the market with a clear vision in a rapidly changing environment through an outline of broad objectives and principles. It seeks to ensure that the Capital Market takes advantage of the full potential, and become a catalyst in the national economic growth and delivery of economic value to the people of Sri Lanka to fulfill their needs and aspirations.

It is envisaged that this Strategic Plan would guide the Sri Lankan Capital Market to be an engine of growth, which facilitates economic development, provides an alternative source of funding, with the ultimate objective of ensuring a strong and vibrant Capital Market in Sri Lanka. In addition to the completion of the planning, the year 2006 marked the launch of the first phase of execution of this Plan and it is with pride that I outline the progress made.

There are 44 developmental activities that have been outlined by this strategic blue print. These developmental activities have now laid a road map for the next 10 years for the Sri Lankan Capital Market. We have segmented the Plan into stages and the first stage of development will include introduction of derivative products to the Sri Lankan Capital Market, listing 10-20 large companies, introduction of an automated surveillance system, creation of the Financial Services Academy, engagement of Employees' Provident Fund (EPF) and Employees' Trust Fund (ETF) in greater participation in the Capital Market, creation of a vibrant Debt Market, creation of the National Wealth Corporation which will deploy a mechanism where docile and less productive government assets will

be shared with the people of the country without losing control of such assets through a economically rewarding mechanism. This will generate higher returns to the savers of this country and get their involvement in the Capital Market of our country. This will also change the average saver of our country to become an investor in the Capital Market.

We have now fast tracked the deployment and introduction of derivatives, since we have found it has the potential to allow investors to diversify their portfolios and hedge their risks whilst boosting the market. With a view to facilitating derivatives trading the SEC is addressing matters relating to a suitable trading system, legal framework and rules, together with prudential supervisory regulations. We are working closely with the National Stock Exchange of India (NSE) in this initiative. We expect to introduce derivatives within a period of one year to the Sri Lankan Capital Market.

In developed Capital Markets Securitisation products account for more than 25% of their Debt Market. In Sri Lanka the lack of proper law and procedure prevents us from engaging in true Securitisation. Therefore we are currently engaged in introducing a new Securitisation law to enable this valuable Debt Market product in Sri Lanka. This involved stimulating discussion with stakeholders, including industry practitioners in regard to tax, legal and administrative processes enabling the introduction of proposed Securitisation Act. We are currently at the stage of drafting the Act for this important legislation.

The SEC in collaboration with the Unit Trust Association of Sri Lanka has taken the initiative to rejuvenate the Unit Trust Industry through awareness building, developing distribution channels and new products. This scheme recognises the pivotal role that the Unit Trust Industry could play in creating wealth among the masses of Sri Lanka. Currently, SEC is contemplating in financially assisting the Unit Trust Industry to ignite its revival through an aggressive plan.

To ensure good Corporate Governance among listed companies and boost investor confidence the SEC and the Institute of Chartered Accountants of Sri Lanka

in consultation with the Colombo Stock Exchange commenced a joint initiative to formulate standards on Corporate Governance. The rules drafted during the course of the year would be made mandatory for listed companies as these standards are to be incorporated into the Listing Rules of the Colombo Stock Exchange. These will include mandatory requirements for all listed companies pertaining to the appointment of Non-Executive Directors, Independent Directors, formulation of audit and remuneration committees together with enhanced disclosure requirements. This is the first time where Corporate Governance has been made mandatory for all listed companies and we will look at consolidation and enhancement of these requirements to the future.

Having realised the need to have a robust surveillance system to enhance investor confidence and ensure a fair marketplace devoid of manipulation and abusive practices, the SEC conducted a thorough review to identify an appropriate surveillance system. Currently discussions are underway with short listed vendors and software developers for procurement of a system in line with our requirements.

The SEC is currently exploring the possibility of embracing an electronic reporting system to enable listed companies and Market Intermediaries to file reports and other regulatory filings electronically. It is envisaged that this will replace the paper-based reporting system and lead to a more efficient, timely and cost efficient system.

In an attempt to enhance the knowledge of professionals and the public on the Capital Market, a comprehensive business plan was drafted for the establishment of the Financial Services Academy. The FSA is entrusted with the task of promoting training and education and will play a pivotal role in enhancing the level of awareness among a wide-ranging audience. FSA will be involved in many programmes including professional education programmes such as the Diploma in Capital Markets, licensing and certification of Stockbrokers, investor awareness programmes together with conducting of specialised programmes.

The aggressive development strategy adopted through the Capital Market Master Plan, resulted in the need to strengthen the Secretariat and its capabilities. Furthermore, in addition to the Stock Exchange, Stockbrokers and the Unit Trust Management Companies, the SEC has been vested with the responsibility to regulate Market Intermediaries such as Underwriters, Margin Providers, Credit Rating Agencies, Investment Managers, Clearing and Depository Houses. During the year, we recruited a significant number of competent professionals from diverse disciplines to effectively support our expanding regulatory, enforcement and development role. Our staff cadre grew by 25% over the year. This resulted in SEC initiating action to relocate the Secretariat to the 28th and 29th floors of the World Trade Center, which will offer better working atmosphere and conditions.

We have also undertaken the responsibility to amend the SEC Act as well as the Takeovers and Mergers Code in line with current needs of the industry. A study has already commenced to look at international legislation in this regard. These proposed amendments will strengthen the legal framework of the Capital Market of Sri Lanka.

Our people are our most important resource. In an endeavour to enhance and fully utilise the capacity and abilities of our staff, we provided regular training opportunities both locally and internationally to increase their professional competence. We greatly encourage them to pursue higher studies in order to enrich their knowledge and capabilities. We believe our investment in people will be a key driver that will significantly contribute towards the successful deployment of our future aspirations.

All these initiatives, we believe, will significantly support the enhancement of market capitalisation of Sri Lanka, paving the way to strengthen our intermediary network through reduction of risk together with the broad basement of the Capital Market with the people of our country.

Lastly, I wish to thank the Chairman and Members of the Commission for their valuable contribution, support, advice and guidance, which was provided to us in a graceful manner. We also thank all Commission Members for the trust and confidence that was bestowed on us. Your keen

interest in our developmental agenda and commitment towards its deployment has significantly motivated us to attain noteworthy achievements in 2006.

I thank the staff for their relentless commitment, enthusiasm and dedication in which they worked as a team in fulfilling the aspiration of all the stakeholders in the Capital Market of Sri Lanka. It has been a rewarding experience for all the staff members to be a part of this challenging developmental agenda, which has been set in motion to take the Capital Market of Sri Lanka to a much higher elevation.

Finally I thank all stakeholders for the valuable support extended to us in taking the Sri Lankan Capital Market to unprecedented heights in the year 2006.


Channa de Silva

Macroeconomic Commentary

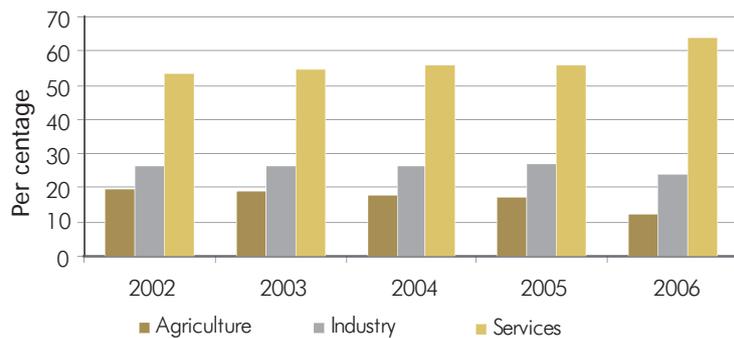
Introduction

The Sri Lankan economy has posted impressive gains and recorded a 7.4% growth rate in 2006. In spite of the breakdown of negotiations between the Government of Sri Lanka and the LTTE, all three sectors of the economy grew at healthy rates and the highest ever half yearly growth in the last decade of 8% was witnessed in 2006. The services sector grew by 8.3% while the Industry sector and the Agriculture sector grew by 7.2% and 4.7% respectively. Growth in the economy was fuelled by investments exceeding 28% of GDP mainly in the Manufacturing, Construction and Services sectors. Favourable weather conditions in the Agricultural sector also made a positive contribution to the overall output. In this context, large investments made in the Telecommunication sector, which is a sub sector of Services, is worth special mentioning. Rapid growth in mobile telephony has resulted in one in four Sri Lankans enjoying telephone connectivity, which in turn has substantially contributed, to productivity improvements and national output. The transformation of the telecommunication industry from a monolithic, monopoly structure to a more competitive industry with private sector participation has resulted in better operational efficiency and a greater degree of responsiveness to consumers.

Fiscal Sector Developments

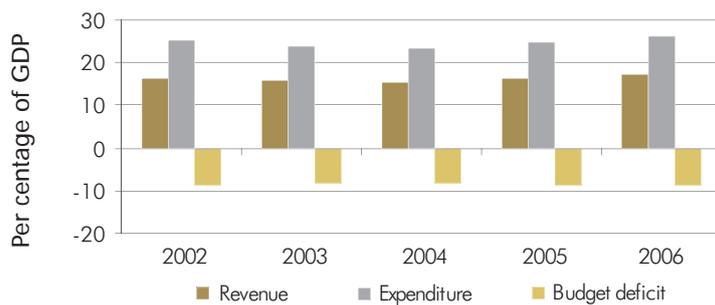
The overall deficit was 8.4% of GDP. Total revenue remained at 17% of GDP while there was a sizable overrun in recurrent expenditure of about 1.1% of GDP, which was due to higher

Sectoral Contribution to Growth



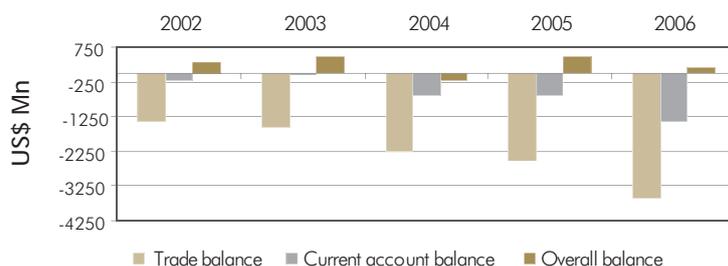
Source: Central Bank of Sri Lanka

Fiscal Sector Development



Source: Central Bank of Sri Lanka

Balance of Payments



Source: Central Bank of Sri Lanka

wages, pensions and subsidies. Capital expenditure fell short of targeted amounts because of slower disbursement of foreign-funded projects. Meanwhile, total government debt to GDP declined to 93% in 2006 from 93.9% in 2005.

Inflation

The persistent budget deficit and partial monetisation thereof, coupled with high global crude oil and other commodity prices, the inflation rate in the country edged up gradually and in November 2006 peaked to 19.8% as measured by the point-to-point Colombo Consumer Price Index (CCPI). This has been the single most worrying aspect of the Sri Lankan economy in the year 2006. Expenditure on unproductive, indeed destructive, activities such as the armed conflict can only add to both cost push and demand pull inflationary pressures. Demand created by Dollar remittances may also be adding to such inflationary pressures and making life difficult for those who are dependent on Rupee wage earnings. To contain inflationary pressures, the government adopted a tighter monetary policy, resulting in bringing down the growth in money supply to about 16.8% by October 2006.

National Savings

Given the above mentioned high inflation, it is perhaps not surprising that the domestic savings rate remain poor at 17.3% of GDP. The savings from remittances from the Sri Lankan workers in the Middle East would add another 6.1%. However, this capital formation (23.4% of GDP) is inadequate to fund investments required to fuel envisaged 7% to 8% GDP growth. Therefore, the remaining capital must come from foreign sources by way of Foreign Direct Investments (FDI) or Portfolio Investment.

Another notable aspect of domestic savings in Sri Lanka is that the bulk of these savings are with the traditional banking system in savings deposits yielding returns much below forecast inflation. Credit risk free T-Bills have often yielded above bank deposit rates. The one year T-Bill rate started the year at 10.50% p.a. and ended the year at 12.98%.

The challenge for the relevant market players is to educate the saving public to shift their savings from low yielding bank deposits and savings accounts to higher yielding

Capital Market instruments including T-Bills. This is a win-win situation for both the saver and the borrower as savers will get better returns and borrowers can raise funds at a lower cost.

External Sector

The overall Balance of Payment (BOP) is projected to record a surplus of US\$ 204 Mn. Export earnings increased by 8.4% while imports grew by 15.7% due to a higher growth in intermediate and investment goods. Due to soaring oil prices, payments for petroleum imports increased by 46.2% during the first eight months in 2006. Worker remittances reached US\$ 2.3 Bn, once again easing the pressure exerted on the BOP. Foreign Direct Investment in the country also showed some improvement ending the year with a total inflow of around US\$ 604 Mn. Due to the resumption of hostilities and violence, the tourist arrivals (from Western Europe) declined and tourist Dollar inflows remained stagnant.

Exchange Rate

The Sri Lankan currency depreciated around 5.2% against the US Dollar, which was expected by the market participants, exporters and importers alike. This can be regarded as not too drastic given the average domestic inflation vis-à-vis that of other economies of our trading partners and the high price of petroleum prices in the global market on which Sri Lankan economy is fully dependent. High level of foreign currency remittances amounting to US\$ 2.3 Bn, mainly originating from the large Sri Lankan labour force employed in the Middle Eastern countries also helped the rupee hold off further depreciation.

Asset Prices

An increasing trend was observed in the last few years in the price movement of land, property and equity surpassing the rate of inflation giving owners of such assets a comfortable hedge against inflation. The demand for apartments in high rise buildings in Colombo and suburbs was buoyant throughout the year. The Equity Market recorded all time highs anchored by growth in corporate profitability and the stability of the political environment. Even the value of motor vehicles increased due to currency depreciation and additional government taxes/duties but there was no drop in demand for passenger vehicles.

Banking vs. the Capital Markets

The banking sector in Sri Lanka is well developed and well regulated. However, the cost of financial intermediation remains high, estimated at 6% to 7%. This is due to various inefficiencies inherent in the banking sector, of which 50% is controlled by state owned banks. Capital Markets are the answer to reducing intermediation cost.

In most developed countries, the financing raised through Capital Markets exceed that raised through the banking system at a 3:1 ratio. In other words, disintermediation level in a well organised economy is high. In Sri Lanka, this proportion is 29% to 71% due to the less developed nature of the Capital Markets. If the funds raised by the Treasury is excluded from the equation, funds raised through the Capital Market by the private sector in Sri Lanka is negligible. This presents a good opportunity for the Sri Lankan corporates to raise lower cost funds. For the investor, it presents an opportunity to get a higher return for their savings. From a macroeconomic perspective, the Capital Markets will give rise to a better allocation of scarce capital to the most productive areas in the economy.

Looking Ahead

The growth momentum that prevailed in 2006 is expected to continue in 2007, and in turn lead to growth in the Colombo Stock Market (CSE). The fiscal deficit and inflation remain the major concerns from a macroeconomic standpoint. The implementation of the Capital Market Master Plan is expected to improve market capitalisation, liquidity issues etc. in the CSE. Fiscal deficit can be contained from any further deterioration by broad basing revenue sources through increasing the number of individual and corporate taxpayers and exercising discipline in expenditure. The challenge for the economy is to bridge the domestic savings shortfall from required level of investment by encouraging foreign capital (official or private) inflows and directing them mainly towards infrastructure development such as roads, railways, ports and power generation.

Capital Market Performance

Equity Market

The Colombo Stock Exchange reflected strong investor resilience and continued to grow despite the renewed hostilities between the LTTE and the government forces. The investors seem to have got accustomed to these factors and has grown steadily throughout the year, becoming one of the best performing markets in the region. Contributions from foreign institutional investors and local investors anchored by robust corporate results enabled the market to surpass many of the records set in the past.

The equity market started the year on a very bullish note and this trend continued upto mid April 2006. In April the market took a breather and was very volatile till the end of August 2006, due to the unfavourable security situation in the country. The market recovered in September and held its ground thereafter. A strong bullish sentiment was created in September with the announcement made by the LTTE to resume peace talks. This propelled the market to recover lost ground and from September the market surged ahead with renewed vigour. Strong quarterly corporate earnings propelled positive sentiments in the market and the ASPI and the MPI soared to new heights of 2,789.78 and 3,795.21 points respectively on 1st December 2006.

The All Share Price Index (ASPI) opened the year at 1,922.21 points and closed the year at 2,722.36 points recording a massive increase of 800.15 points. The more liquid Milanka Price Index (MPI) opened the year at 2,451.06 points and closed the year at 3,711.80 points, recording an increase of 1,260.74 points. Accordingly, the ASPI recorded a significant growth of 41.62% whilst MPI had a stellar increase of 51.43% at the end of 2006.

However, the turnover for the 241 trading days in the year 2006 was lower than in the previous year, recording Rs. 105.15 Bn, which is a decline of 8.24% compared to Rs. 114.60 Bn achieved in the year 2005. Domestic investors accounted for 67.2% of the total equity turnover in 2006, while foreign participation accounted for 32.8%. The net foreign inflow amounted to Rs. 5.4 Bn, while in the previous year, it amounted to Rs. 6.1Bn.

The highest daily equity turnover for the year, of Rs. 3 Bn was recorded on 15th November 2006 and trading of SLT accounted for over half the day's turnover. Further, in the year under review due to strategic deals and high foreign and local interest in blue chips such as Dialog Telecom, Sri Lanka Telecom and John Keells Holdings the market witnessed frequent increase in turnover per day of over Rs.1 Bn.



Source: Colombo Stock Exchange

Capital Market Performance contd...

During the year under review, Price Indices of 17 sectors recorded growth, while 3 sectors declined. The Motors sector recorded the highest growth of 118% whilst the Plantations sector and the Chemicals & Pharmaceuticals sector grew by 74.6% and 73% respectively. In 2006 the highest decline of 18% was witnessed by the Power and Energy sector.

The market capitalisation of the Colombo Stock Exchange at the end of the year stood at Rs. 834.76 Bn, which is approximately 30.0% of GDP.

In 2006 the mini-hydro power company, Vallibel Power Erathna Ltd was listed on the second board of the bourse by way of an IPO and Amana Takaful, the insurance arm of Amana Investments obtained a listing through an introduction. Another significant incident that took place in the Colombo Stock Exchange in the year under review was the admittance of five new brokers to trade in debt and equity.

The single overriding factor inhibiting the sustainable development of the Capital Markets has been the conflict in the North and East and its effect on investor confidence and the economy as a whole. Other broader issues from an international perspective include the lack of liquidity and limited market size.

Debt Market

There were 2 issues of listed debentures during the year 2006. The corporate debt turnover for the year amounted to Rs. 405.2 Mn, reflecting a significant increase from 2005. A total of Rs. 2.4 Mn worth of debentures were traded during 2006.

Transactions in the Secondary Market of government securities declined during 2006 perhaps due to expectations of an upward movement in the interest rates. The number of government securities traded in the period under review amounted to Rs. 213.2 Mn while the turnover amounted to Rs. 207 Mn on the DEX System.

Unit Trusts Funds

The Unit Trust Industry recorded a positive growth of 19% in terms of the fund value, 3% in units issued, whilst the number of unit holders recorded a negative growth of 1% in comparison to the previous year.

The Overall Position of Unit Trust Funds as at 31 December 2006 and 31 December 2005.

	31 December '06	31 December '05	Change
Net Asset Value (NAV) (Rs.Mn)	5,352	4,495	19%
No. of Unit Holders	23,417	23,654	(1%)
No of Units Issued (ooo)	355,553	345,528	2.90%
Investment in Equity (Rs.Mn)	3,700	2,983	24.04%
Investment in Treasury Bills (Rs. Mn)	956	1,327	(27.95%)
Investment in other Instruments *	696	185	276.21%
ASPI	2,722.36	1,922.21	41.64%
MPI	3,711.80	2,451.06	51.44%

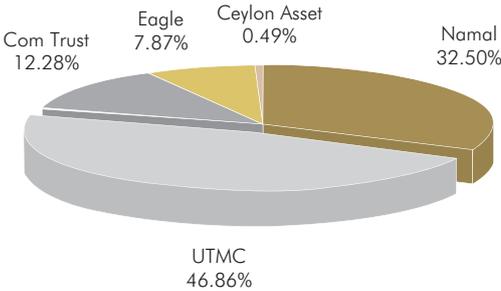
Source: Unit Trust Management Companies

* (E.g. Commercial Papers, Promissory Notes, Debentures and Bank Deposits)

At the end of the year 2006, 356 Mn units were in circulation compared to 346 Mn units in 2005, pertaining to the 13 Unit Trust Funds. The number of unit holders had decreased from 23,654 as at 31 December 2005 to 23,417 as at 31 December 2006. The overall Net Asset Value of the Funds increased by Rs.857 Mn (approx.) from Rs. 4495 Mn (approx.) to Rs. 5352 Mn (approx.) as compared to the previous year. The main reason for the increase in the NAV was due to the increase in the NAV of Balanced and Growth Funds, which invests heavily in the Stock Market. This was in line with the increase in the ASPI and the MPI of 41.64% and 51.44% respectively.

It was also observed that 69% (approx.) of the deposited property of Unit Trusts had invested in the Equity Market and 18% (approx.) of their funds in Treasury Bills, whilst 13% (approx.) was invested in other Money Market instruments.

Market Share of the Unit Trust Management Companies



Operational Review



Operational Review

Supervision

Stock Broking Companies

The SEC Act requires all Stock Broking companies to obtain a license in order to be members of a licensed Stock Exchange. The license is granted by assessing the financial position, compliance with the Colombo Stock Exchange (CSE) Member Regulations and requirements pertaining to liquidity and net capital. In addition, on-site supervision is conducted annually to determine the financial stability of the Stock Broking Firms.

In order to ensure financial viability the SEC has stipulated that the Stock Broking companies maintain a minimum net capital requirement of Rs. 15 Mn. This requirement will be increased to Rs. 25 Mn with effect from 31 December 2006. Off-site inspection carried out by us revealed non-compliance by four companies that resulted in immediate action being taken to rectify the net capital requirement.

In addition to the minimum net capital requirement, Stock Broking companies are obliged to adhere to requirements of liquidity, appointment of competent compliance officers capable of overseeing regulatory procedures and maintain separate client accounts. These companies are required to submit monthly-unaudited accounts, net capital statements, debtors and creditors age analysis and liquidity position to the Commission, which are analysed to ensure financial performance and stability. Further, compliance reports are submitted to the Commission and are reviewed by the officers of the Supervision Division to ensure compliance procedures are adhered to, whilst the monthly-unaudited accounts are analysed to ensure that the Broking Firms are financially stable.

We visited the fifteen Stock Broking companies during the year to ensure that the companies complied with the SEC Act and rules of the CSE. During on-site supervision, it was observed that a few companies had internal weaknesses such as inadequate Management Information Systems and portfolio balances, inaccurate net capital calculation and granting of extensive credit to clients. However other than the aforesaid weaknesses, the Stock Broking Companies were found to be satisfactory.

In the year under review licenses of 15 Stock Broking companies were renewed and new licenses were issued to five Trading Members. As a result the number of Stock Brokers increased from 15 to 20 during 2006.

Unit Trust Management Companies

There were 13 Unit Trust Funds managed by 5 Management Companies as at 31 December 2006. In order to verify whether the investment parameters for Unit Trust Funds were maintained as set out in the Unit Trust Code and Trust Deeds, on-site inspection was carried out of the five Unit Trust Management Companies in accordance with the audit programme. Inspections were also undertaken to ensure strict compliance with operational procedures and ascertain the financial stability of the companies concerned.

We reviewed the monthly accounts and returns submitted to the Commission in respect of the 13 Unit Trust Funds. In addition, the exposure levels were monitored of the Unit Trusts according to the investment limitations set out in the Trust Deeds and the Unit Trust Code. The Companies were found to be within acceptable exposure limits.

A Management Company that was found to have fallen below the minimum net capital requirement due to losses incurred during 2006, was provided time to correct this position by infusing the required capital.

In addition the Supervision Division received and approved advertising materials, press releases, interim reports and annual financial statements of the Funds and Management Companies.

Market Intermediaries

The SEC Act was amended to empower the Commission to grant a Certificate of Registration to a person to carry out business as a Market Intermediary and to ensure the proper conduct of such business.

During the review of audited accounts and interim accounts, it was observed that a few Market Intermediaries did not meet the stipulated minimum net capital and liquidity requirements and were requested to infuse the shortfall. Subsequently a number of companies rectified their positions. Furthermore, two Market Intermediaries were requested to cease operations due to non-compliance with financial requirements.



Registration and Licensing

	Licenses		Registrations	
	Renewals	New	Renewals	New
Stock Brokers	15			
Stock Dealers	03			
Stock Broker/ Stock Dealer		05		
Credit Rating Agencies			2	
Clearing House			1	
Investment Manager			9	3
Margin Provider			13	2
Underwriters			4	

Strengthening the Legal Framework

Corporate Governance

Pursuant to a joint initiative by the Institute of Chartered Accountants of Sri Lanka and the SEC, a committee formulated rules on Corporate Governance. These Rules will be incorporated in the Listing Rules of the CSE with a view to enforcing mandatory compliance.

The Committee decided to develop standards in respect of the following in the first instance:

- Non-executive directors
- Independent directors
- Criteria for determining 'independence' of directors
- Disclosure by directors
- Remuneration committees
- Audit committees

It is envisaged that these rules will be implemented in the following manner.

- It will be mandatory for listed companies to publish a Table in the Annual Report relating to the financial year commencing on or after 01st April 2007 confirming that as at the date of the Annual Report they

comply with the Corporate Governance Standards set out in the Listing Rules and if not, explain why the company has not complied with identified items.

- It will be mandatory for listed companies to comply with the Corporate Governance Standards in the Listing Rules with effect from the financial year commencing on or after 01st April 2008 and the Annual Report must contain the relevant affirmative statements.

Takeovers and Mergers

Following the constitution of a Committee in September 2003 the SEC continued with the revision of the Takeovers & Mergers Code 1995 in consultation with the stakeholder committee appointed to carry out this task.

The revision aims at achieving a greater degree of clarity in the provisions made and facilitation of development in the Capital Market. Parallel regulation in the U.K. and in emerging markets in Asia have also been considered for purposes of the revision which is expected to continue in 2007.



Securitisation

Securitisation is utilised as an alternate mechanism to facilitate financing. From an industry stand point it is important to regulate the structuring of securitisation as it involves mobilisation of funds from the public domain.

The SEC has been designated by the Ministry of Finance to liaise with a consultant in drafting a Securitisation law to develop the Capital Market in Sri Lanka.

A diagnostic study was carried out in consultation with industry stakeholders to identify specific needs of the market, the strengths and weaknesses of the regulatory framework and the options available. A document containing the proposed drafting instructions for the new Securitisation Act was issued for public comment.

Rules for Investment Managers, Margin Providers, Credit Rating Agencies, Underwriters and Clearing Houses

Subsisting standards subject to which the five classes of Market Intermediaries are registered was reviewed and a revision thereof completed with the ultimate objective of facilitating professionalism, competence and securing better risk management. We worked in consultation with the industry in this respect and the rules are currently in operation.

Unit Trusts

Parameters and exposure limits pertaining to investments made by Unit Trusts developed in 1992 was subsequently revised in 2006. During the year under review we worked in consultation with industry specialists to revise standards and formulate regulations for Closed End Funds, taking into account the recent developments in the Capital Market. The feasibility of facilitating listing of units on the CSE is also under consideration.



Approvals

Mergers and Acquisitions

The Takeovers and Mergers Code of 1995 as amended in 2003 (Code) apply to takeovers and mergers where the offeree is a listed public company. The Code seeks to ensure equal treatment of all shareholders of the same class in the company sought to be taken over. The rules of the Code are aimed at ensuring dissemination of sufficient information and advice with adequate time to the shareholders of the target company in order for them to arrive at an informed decision relating to the takeover. The Code deals with three types of offers namely Voluntary Offers, Partial Offers and Mandatory Offers. During the year under review we administered one Partial Offer and six Mandatory Offers.

Takeovers and Mergers (January 2006 - December 2006)

Offeror	Offeree	Type of the offer
Janashakthi Limited acting in concert with Mr. Dinesh Schaffter	Central Securities Limited	Mandatory Offer
Janashakthi Limited acting in concert with Nextventures Limited and Dinesh Schaffter	V Capital Limited	Mandatory Offer
John Keells Holdings Limited	Associated Motorways Ltd.	Partial Voluntary Offer
Hemas Holdings Ltd acting in concert with Leisure Asia Investments Ltd, Hemtours(pte) Ltd and Mr. J C L De Mel, Mr. A N Esufally, Mrs. M S Fonseka and Mr. H.N Esufally.	Serendib Hotels Ltd.	Mandatory Offer
Sri Lanka Insurance Corporation Limited	Lanka Hospital Corporation Limited	Mandatory Offer
Specialist Gasses (private) Limited	Ceylon Oxygen Limited	Mandatory Offer
Sri Lanka Insurance Corporation Limited acting in concert with Mr. D K Subasinghe, Ms. S N Subasinghe and Mr. P P Subasinghe.	Asiri Surgical Hospital Limited	Mandatory Offer

Issuance of unlisted securities

Section 29A of the SEC Act requires any listed public company to obtain the prior approval of the SEC before issuing unlisted securities.

The above table indicates the applications which were reviewed and approved under section 29A of the SEC Act by the Commission.

Allotment of shares before obtaining a listing

In terms of Section 28A of the SEC Act, where shares in any public company are allotted to any person prior to its listing in a licensed Stock Exchange, no shares or any security convertible to shares in any such company shall be listed on a licensed Stock Exchange within a period of one year from the date of the last allotment, unless the written approval of the Commission is obtained for that purpose prior to such listing.

During the year under review approval was granted for an application made by Ceylinco Leasing Corporation for a share split of 7,695,590 ordinary shares of Rs. 10 to 76,955,900 Ordinary Shares of Rs. 1 each and a Bonus Issue of 65,962,200 ordinary shares of Rs. 1 each.

Country and Regional Funds

Approval was granted to 81 Regional/ Country Funds to invest in companies in Sri Lanka, in terms of the Gazette Extraordinary No.720/12 of 24th June 1992.

Name of the issuer	Type of the Issue	Amount approved
Mercantile Leasing Limited	Redeemable unsecured debentures	Rs. 500 Mn.
Singer Sri Lanka	Redeemable unsecured debentures	Rs. 800 Mn.
DFCC Bank	Redeemable unsecured subordinate debentures	Rs. 2000 Mn.
Aitken Spence & Company Limited	Redeemable unsecured debentures	Rs. 1000 Mn.
John Keells Holdings Limited	Redeemable unsecured debentures	Rs. 2000 Mn.
The Finance Company Limited	Redeemable unsecured subordinate debentures	Rs. 500 Mn.
Seylan Bank Limited	Redeemable unsecured subordinate debentures	Rs. 1000 Mn.
Sampath Bank Limited	Redeemable Unsecured subordinate debentures	Rs. 300 Mn.

Approval of Off-The-Floor Share transactions

Approval was granted for 383 exceptional transfers and 301 gifting of shares during the year under review. The exceptional transfers were in order to facilitate margin trading, fund management, de-listing and restructuring of entities and portfolios where beneficial ownership remain unchanged.

Other approvals

The Commission approved the decision of the CSE to grant a waiver to DSI Holdings Limited (DSIHL) on rule 1.6 –1d(ii) of section 1 of CSE Listing Rules.

Compliance

All Listed Companies are required to submit Annual Reports within six months from the close of the financial year to their shareholders and the CSE. To ensure compliance with CSE Listing Rules, we reintroduced the process of reviewing Annual Reports of listed companies from September 2006 onwards. The objective of this exercise was to enhance the quality of information disseminated by listed companies. Listed companies are required to disseminate material information promptly in order to establish transparency and accountability in the Securities Market, and to ensure that professional standards are maintained.

This process will contribute 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 reviewing the Annual Reports we focused on the following areas:

- Compliance with CSE Rules, Sri Lanka Accounting Standards (SLAS) and relevant provisions of the Companies Act
- Corporate Governance practices
- Shareholder and investor information
- Financial summary
- Chairman's report
- Audit report
- Financial highlights
- Corporate information
- Management discussion and analysis

Matters relating to non-compliance were communicated to listed companies and they responded positively to this endeavour.



Market Surveillance

Surveillance plays a vital role in preventing trading violations and ensuring market confidence. We continuously monitored price and volume anomalies to detect any market abuse, based on a real time computer assisted surveillance system. Whenever irregular trading activity was detected, preliminary examinations were undertaken to determine the circumstances behind the unusual volume or price movements. The findings of the preliminary examinations were referred to the Investigation Committee to ascertain whether further investigation was warranted.

The SEC requires listed companies to disclose financial and other material information to the public. This provides a steady flow of timely,

comprehensive, and accurate information for proper functioning of the price discovery mechanism. We scrutinised company disclosures, press releases and market rumours to ascertain whether there is any discernible pattern between price movements prior to information being officially disseminated.

During the year under review, we detected 11 cases of possible violations of the provisions of the SEC Act, and examined these further. These findings were referred to the Investigation Committee for further examination and possible enforcement action.

The analysis of such detections in terms of broad categories of violations are listed below:

Nature of Surveillance	No. of issues
Insider Trading	3
Market Manipulation	4
Others	4
Total	11



Litigation

Cases filed by the SEC

Securities and Exchange Commission of Sri Lanka vs. Magpek Exports Ltd. and its Directors

In terms of the Securities and Exchange Commission of Sri Lanka Act (as amended) the Securities and Exchange Commission of Sri Lanka filed charges against Magpek Exports Ltd. and its Directors for failing to immediately disclose material information to the Market and for the creation of a false Market in respect of shares of Magpek Exports Ltd.

Charges against three of the defendants were compounded in August 2001 on an application made in that respect.

The trial against the remaining defendants is continuing in the Magistrate's Court, Fort as at 31st December 2006.

Securities and Exchange Commission of Sri Lanka vs. Mr J.A.S. Piyawardena, Mrs Chandra Piyawardena & Securities and Exchange Commission of Sri Lanka vs. Ms J.A.C.W. Piyawardena

In terms of the SEC Act the SEC filed charges against the abovementioned parties in the Magistrate's Court, Fort, for the offence of having traded in the shares of Nawaloka Hospitals Limited, on the basis of price sensitive information prior to its disclosure to the Market.

Trial against the defendants in the first mentioned matter was to commence in the Magistrate's Court, Fort while summons were to be served in the second matter as at 31st December 2006.

Securities and Exchange Commission of Sri Lanka vs. Mr B. A. Jayasekera and others

In terms of the SEC Act (as amended) the SEC filed charges as follows against the parties mentioned below:

Conspiracy to commit acts to create a false/misleading appearance of an active Share Market (Rule 12 of SEC Rules read with Section 113B and 102 of the Penal Code)

B. A. Jayasekera

D. A. Samaradiwakara

U. H. Dharmadasa

K. M. N. Piyarathne

Michael de Saram

M. T. Ganhewage

L. C. Pallegedera

Mahanama Jayaweera

Jayantha Dharmadasa

committing acts to create a false/misleading appearance of an active Share Market (Rule 12 of the SEC Rules)

B. A. Jayasekera

D. A. Samaradiwakara

U. H. Dharmadasa

K. M. N. Piyarathne

Michael de Saram

M. T. Ganhewage

L. C. Pallegedera

Aiding and abetting to commit acts to create a false/misleading appearance of an active Share Market (Rule 12 of the SEC Rules read with Section 102 of the Penal Code)

Jayantha Dharmadasa

Mahanama Jayaweera

Cases filed against the SEC

Debbie Harding vs Securities and Exchange Commission of Sri Lanka Labour Tribunal (LT) Case No.1/347/02

Termination of the services of Ms Debbie Harding, Confidential Secretary, has been challenged in the Labour Tribunal.

As at 31st December 2006, the trial in this matter is continuing.

Inquiries and Investigations

Amendments to the SEC Act which came into force in 2003, vested us with vital investigative powers, which contributed immensely to facilitate investigations in a more effective and expeditious manner.

A total of 12 investigations were conducted in the year 2006, out of which 8 were completed, while one investigation was suspended. The details of the action taken/current status of the investigations are given in the table:

Nature of Investigation	No. of Investigations	Action Taken/Current Status
Insider Dealing ¹	04	<ul style="list-style-type: none"> Two matters which were referred to the Attorney General's Department for a formal opinion were pending at the end of the year 2005. During the year under review these matters were concluded, based on the advice received from the Attorney General's Department. The SEC instituted Legal Action in terms of the SEC Act No. 36 of 1987 as amended based on the findings of an investigation. The preliminary investigation report pertaining to an investigation was referred to the Attorney General's Department for formal advice and has not yet been concluded.
Market Manipulation ²	06	<ul style="list-style-type: none"> Offence against an individual was compounded for a sum of Rs. 550,000/- for an investigation which was concluded in 2004 A report incorporating the advice given on an investigation, by the Attorney General was submitted to the Members of the Commission. The Commission recommended reprimanding the parties involved in market/price manipulation. The SEC instituted Legal Action in terms of the SEC Act No. 36 of 1987 as amended based on the findings of an investigation. Subsequent to detailed investigations, two investigations were terminated due to lack of evidence to establish charges of Market/Price Manipulation. An investigation was terminated owing to the reason that the individual suspected to have engaged in Market/Price Manipulation is one of the defendants of a legal action instituted by the SEC for manipulating the market/price in relation to the shares of some other listed company. At the end of the year 2006, investigation relating to one case was in progress.
Complaint against a Stock Broker	01	<ul style="list-style-type: none"> Deliberation relating to one complaint was suspended until the finality of certain on-going litigation since the issues pertaining to the said complaint form the subject matter of the litigation.
Forgery/Cheating	01	<ul style="list-style-type: none"> An Investigation to establish forgery/cheating was terminated due to lack of evidence.



¹ 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 Creation of a false or misleading appearance in respect of the trading, or the price of any securities listed on a stock market.

Complaints

We received 29 complaints related to the following matters during the year under review.

Nature Of The Complaint	Number	Resolved	Pending
1 Complaints against brokers	11	10	1
2 Unauthorised transactions	4	4	-
3 Breach of CSE Listing Rules	8	8	-
4 Rights Issues/Bonus Issues/Dividends Payments	4	4	-
5 Opening of CDS Accounts/Registration of Shares	2	2	-
TOTAL	29	28	1

Market Development Initiatives

Consultancy to develop a Corporate Bond Market

Considering the thin growth of the Corporate Debt Market in Sri Lanka, in contrast to the Equity market, the SEC obtained the services of a consultant to prepare a detailed plan of action to develop a vibrant Debt Market in Sri Lanka. Discussions were held with Debt issuers, Investors and Intermediaries and their suggestions were considered when preparing the final report. The consultant presented his report to the Secretariat in June.



Market awareness and training

Title	Participants	Venue
Capital Market of Sri Lanka	Undergraduates	Universities of Colombo and Sabaragamuwa
	Bank Staff	Seylan Bank Training Institute
	Members of the Tea Commissioner's Department	Gampola
	Media personnel	Colombo
	Education Directors/Assistant Directors	Kandy and Nuwara-Eliya Educational divisions
	Advanced Level students	Uva, North-Central provinces, Puttalam, Dehiyathakandiya and Hagaranketha Educational Zones.
	Benefits of Investing in the Stock Market	Sabaragamuwa Chamber of Commerce & Industry staff
Members of the Institute of Engineers- Wayamba		Kurunegala.
Members of the Bandarawela Traders Association		Bandarawela
Members of the Bar Association-		Kurunegala
Members of the Construction Association		Kurunegala
The potential of the Colombo Stock Market	Members of the Rotary Club	Kurunegala.
	Members of the Women Lawyers' Association	Holiday Inn -Colombo
	Members of the registered doctors of the Wayamba Region	Kurunegala
The responsibility of senior managers & accountants after an IPO	Senior Managers - DSI Group	Colombo
Capital markets and its current developments (four three-day residential training programmes)	Regional Master Teachers, Resource Teachers and Additional Directors of education	NIE auditorium Maharagama, with field visits to the Colombo Stock Exchange and the SEC
"Investor Day" programmes	Potential investors	Matara, Badulla and Kuliyaipitiya
Enforcement Support Programme (Operational aspects of the Financial Intelligence Unit)	Representatives from the IOSCO Asia Pacific Regional Committee (APRC) countries and stakeholders of the Capital Market	Colombo Hilton

Research

In order to cultivate widespread savings habit and encourage the participation of the rural populace in the Capital Market a study was undertaken to evaluate the possibility of establishing the National Wealth Corporation (NWC) to which the government has pledged its commitment in the Budget 2007.

To foster awareness and encourage investment in Unit Trust Funds among non-nationals, the Division undertook a study to ascertain the investment opportunities available and the shortcomings faced in the repatriation of funds.

To make use of the expertise and resources available within Universities the Division initiated a project, which invites undergraduates and graduates to undertake various research assignments pertaining to topics of interest related to Capital Markets in Sri Lanka.

Re-positioning the SEC - Capital Market Master Plan

The Capital Market Master Plan was developed in collaboration with Ernst and Young Malaysia as a project funded by the Asian Development Bank. The plan was based on a series of consultations held with Government Ministries and Capital Market stakeholders. This maps the future direction of the Sri Lankan Capital Market for the next 10 years from 2006 through 2015. The Master Plan aims to enhance the development and performance of the Sri Lankan Capital Market ensuring that it is well positioned to support Sri Lanka's economic development and wealth

creation among the urban and rural populace. The development of the Capital Market will be carried out over four phases. The year witnessed the ground work being laid to establish a Programme Management Office, in which the ultimate responsibility of implementing the plan would be vested.

National Equity Wealth Distribution Scheme

A key recommendation identified to be implemented in the first phase of the CMMP is the establishment of National Wealth Corporation Ltd, for which official sanction has been given through the passing of budget 2007 by Parliament with an overwhelming majority. One of the main objectives of the NWC is to create wealth amongst the rural masses in the country in the long run through a conduit of Unit Trusts and cultivate a long-term investment and savings culture in the country.

The Financial Services Academy

The CMMP in its endeavour to enhance the knowledge of professionals in the Financial Services Sector recommended the creation of an institute which will identify the educational needs of the Capital Market and the insurance industry. In line with this recommendation a comprehensive business plan was drafted for the establishment of the Financial Services Academy (FSA). The primary focus of the FSA is to enhance skills training and development in the Financial Services Sector, building the necessary competencies that are needed to keep abreast of new developments taking place within the industry on a continuing basis.

International Relations

South Asian Securities Regulators' Forum

The first South Asian Securities Regulators' Forum was held on the 23rd and 24th August 2006 in Colombo. Eight delegates representing five South Asian countries participated at this event. Mr. Nivard Cabraal, Governor, Central Bank of Sri Lanka participated as the Chief Guest at the inauguration ceremony which was held on the 23rd evening at the Cinnamon Grand, Colombo. The deliberations of the forum were held on the following day.



Human Resources

Staffing

In the light of new development initiatives the SEC increased its cadre by creating the positions of Deputy Director General, 1 Director, 4 Assistant Directors and 8 Executives. Action has already been taken to strengthen the SEC by sourcing human resources externally whilst facilitating internal promotions whenever possible. During the year under review 7 Executives and 1 Officer was recruited.

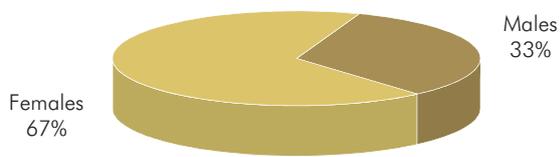
In order to foster relationships among other regulatory bodies SEC seconded two members of the staff to the Insurance Board of Sri Lanka and one Director to the Financial Intelligence Unit of the Central Bank of Sri Lanka.

The approved cadre and the Human Resource strength of the Secretariat as at 31.12.2006 is depicted below.

Post	Approved Cadre	In Employment
Director General	01	01
Deputy Director General	01	-
Directors	09	06
Assistant Directors	04	01
Executives	30	23
Non Executives	17	10
Support Staff	07	07
Total	69	48

As at 31st December 2006 the SEC had 48 staff members that served the Commission consisting of 16 males and 32 females. The gender, age and service analysis of the staff of the SEC is as follows.

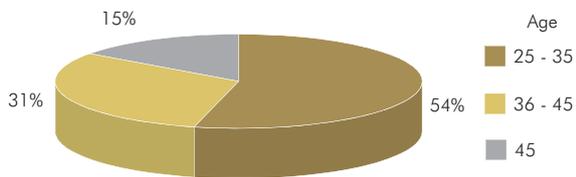
Gender Analysis 2006



Age Analysis

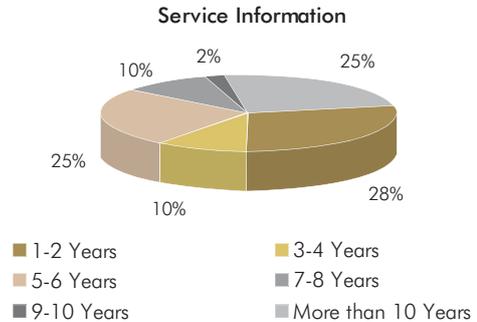
Age Group	Number of Employees as a % of total employees
25-35 Years	54%
36-45 Years	31%
46- 55 Years	15%

Age Analysis



Service Information

Period of Service (years)	No. of years of Service
Up to 2	28%
3-4	10%
5-6	25%
7-8	10%
9-10	2%
More than 10	25%



Training

The Secretariat continued to place emphasis on the development of technical skills of the staff in their relevant fields to discharge the mandate entrusted to the Commission effectively and efficiently. The foreign training provided during the year covered programmes such as the 7th Annual Emerging Markets Programme Malaysia, APEC Financial Regulators Training Programme Malaysia, Tokyo Seminar on Securities Market Regulation, Supervisory Management Programme Singapore, Toronto Centre Securities Supervisory Programme Canada etc. Local training too was provided to all levels of staff that included a residential programme on 'Team Building' at the Bentota Beach Hotel. The total cost incurred on local and foreign training for the staff of the SEC during the year under review amounted to approximately Rs. 6.9 Million.

Staff Welfare

Secretariat offers its staff a range of benefits such as indoor and outdoor medical schemes, personal accident insurance cover, vehicle and distress loan schemes, festival advance, educational grants and reimbursement of membership fees to professional bodies etc.

The Secretariat continuously provide opportunities to the staff and their families to interact whilst advocating harmonious relationships between families by organising a Sports Day, Residential Training Programme, Pirith Ceremony and the Annual Christmas Party.

On the Sports Day the staff of the SEC extended their joy to a few under privileged children by making them participate on the said day. Presents and many surprises were organised for all the children.



Information Technology

Unit on Information Technology continuously supported the functions of the Secretariat whilst undertaking the initiative to archive important documents from the inception of the SEC to an electronic media with appropriate access controls.

To strengthen the surveillance function we have acquired, Bloomberg Financial System, an integrated platform that streams together real-time and historic price data, financial statistics, news and other professional analytic tools.

Relocation of the Secretariat

Initiated action to relocate the SEC Secretariat to the 28th and 29th floors of the World Trade Center in order to enhance the corporate image whilst establishing a state of the art office. This office will offer comfort and ambiance for the professionals to engage in their work in a more productive manner.



Statutory Funds

Cess Fund

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

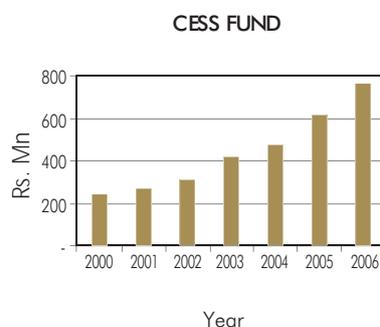
- 14 (A) (1) There shall be charged, levied and paid a Cess at such rates as may be specified by the Minister by order published in the Gazette on every purchase and sale of securities recorded in a licensed stock exchange or notified to it under its rules by both the purchaser and the seller. Different rates may be specified in respect of different classes of securities.
- (2) The Cess imposed under this Section shall be in addition to any other tax or Cess levied under any other written law.
- 14 (B) (1) There shall be established a fund called the Cess Fund to which shall be credited the proceeds of the Cess imposed under Section 14A.
- (2) There shall be paid out the Cess Fund such sums as may be authorized by the Commission for the purpose of-
- (a) developing the securities market;
 - (b) enhancing monies lying to the credit of the Compensation Fund established under section 38; and
 - (c) exercising, performing and discharging the powers, duties and functions of the Commission for the purpose of achieving its objects.

- (3) The money lying to the credit of the Cess Fund may be invested by the Commission in such manner as may be determined by the Commission.

The rate of Cess charged by the SEC was reduced from 0.1% to 0.09% per transaction with effect from 1st December 2003.

Cess on Intra Day Trading - Intra day trade is where a client buys and sells or sells and buys the same security on the same day through the same broker. As at February 2006 Cess on Intra day trades of clients will not be charged on one side of the transaction as set out below;

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

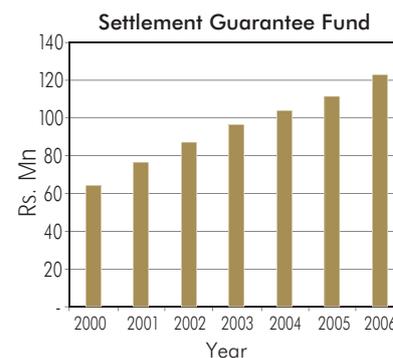


The balance lying to the credit of the Cess Fund as at 31st December 2006 amounted to approximately Rs. 775 Mn.

The Settlement and 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 described below.

- The settlement cycle presently followed by the CSE is of a two-tiered nature.
- Ownership of shares traded is transferred no sooner a trade is executed. With effect from 3rd October 2005 the settlement cycle for equity transactions was reduced. Accordingly the buyer is required to pay on T+3 i.e. on the 4th market day including the day of trading and the seller to settle on T+ 4 i.e. the 5th market day including the day of trading. This relatively long interval between transfer of ownership and receipt of proceeds that gave rise to an unsecured settlement risk necessitated the establishment of SGF.
- The Trustees of the Fund hold office as ex-officio and comprise the Chairman of SEC, the Chairman of CSE, the Deputy Secretary to the Treasury, the Director General of SEC and the Director General of CSE.
- The Government of Sri Lanka has contributed a sum of Rs 50 million to the said Fund. This money has been invested in Government securities in terms of the Trust Deed. SGF can also receive donations, gifts and endowments as replenishments. The broker/custodian banks are presently not required to contribute to the Fund.
- The balance lying to the credit of the fund as at 31.12.2006 amounted to Rs 122 Mn.

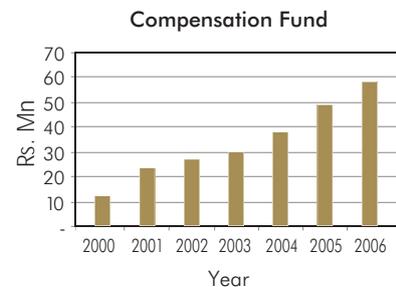


Compensation Fund

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

- There shall be established a fund called the Compensation Fund, for the purpose of granting compensation to any investor who suffers pecuniary loss as a result of any licensed stockbroker or licensed stock dealer being found incapable of meeting his contractual obligations.
- The Compensation Fund shall consist of;
 - Such sums of money as may be voted upon by Parliament for the purpose of the Fund.
 - Such sums of moneys may be credited to the Fund under Section 51A; (Section 51A is on compounding offences)
 - Such sums of money as may be credited from Cess Fund under section 14B.
- Moneys belonging to the Compensation Fund may be invested by the Commission in such manner as may be determined by the Commission.
- The Minister shall appoint from among the members of the Commission three members who shall comprise the Compensation Committee.
- The Committee shall be responsible for assessing and awarding compensation in respect of any application made and the decision of such Committee on any such assessment or award shall be final and conclusive for the purpose of this Act.
- The Act also provides for the procedure for applying for compensation. According to the Act, the Committee may, after examination of the documents and other evidence produced in support of the claim by an applicant, or in any case where an inquiry was held on the conclusion of such inquiry, allow or disallow such claim for compensation. Up-to-date there have been no claims made from the Compensation Fund.

The balance lying to the credit of the Compensation Fund as at 31.12.2006 amounted to approximately Rs. 58 million including Rs 3.85 Mn received for compounding offences pertaining to contravention of provisions of rules made under the Act and market/price manipulation and insider dealing during the year under review. The growth of the Fund during the period 2000 to 2006 is as follows.



Financial Statements and Statistics



Balance Sheet

as at 31st December 2006

	Notes	As At 31.12.06 Rs.	As At 31.12.05 Rs.
ASSETS			
NON CURRENT ASSETS			
Property Plant & Equipment	1	19,870,853	24,093,739
Cess Fund	2	7,782,473	8,092,397
CURRENT ASSETS			
Inventories	4	304,944	400,788
Receivables	5	975,707	854,585
Cess Fund	2	767,937,088	610,501,891
Compensation Fund	3	58,139,793	49,459,089
Deposits, Advance and Prepayments	6	1,741,350	933,935
Repo Investments - Life Insurance Payable	7	-	5,636,627
Cash & Cash Equivalents	8	17,114,102	7,042,966
TOTAL ASSETS		873,866,310	707,016,017
FUNDS AND LIABILITIES			
FUNDS EMPLOYED AND RESERVES			
Reserves	9	26,407	1,731,840
Accumulated Fund	10	5,027,338	(1,797,388)
Cess Fund	11	775,659,191	618,594,288
Compensation Fund	12	58,120,097	49,459,089
NON CURRENT LIABILITIES			
Lease Creditor	13	5,360,241	4,566,913
Grant - Capital Expenditure from Cess Fund	14	12,821,739	18,269,284
Retirement Benefit Obligation	15	5,848,892	5,161,801
CURRENT LIABILITIES			
Cess Fund	2	60,370	-
Compensation Fund	3	19,696	-
Creditors & Accruals	16	7,936,325	2,621,281
Life Insurance Payable	7	-	5,636,627
Receipts in Advance		514,122	409,729
Current Portion of Lease Creditor	13	2,471,892	2,362,553
TOTAL FUNDS AND LIABILITIES		873,866,310	707,016,017

The Accounting Policies and Notes appearing on pages 44 to 55 form an integral part of the Financial Statements. The Members of the Securities & Exchange Commission of Sri Lanka are responsible for the preparation and presentation of these Financial Statements.

FOR AND ON BEHALF OF THE SECURITIES AND EXCHANGE COMMISSION OF SRI LANKA


Channa de Silva
DIRECTOR GENERAL


Gamini Wickramasinghe
CHAIRMAN

Colombo.
27th March 2007

Income and Expenditure Statement

for the year ended 31st December 2006

Income	Notes	Year Ended 31.12.06 Rs.	Year Ended 31.12.05 Rs.
Broker License Fees		603,307	431,898
Unit Trust License Fees		-	230,000
Administration Levy		1,210,999	336,290
Sale of Publications		13,500	33,750
Management Fee		380,429	1,496,375
Sundry Income		115,962	42,581
Profit on Disposal of Property, Plant & Equipment		1,969,494	562,992
Recognition of Grants	14	7,884,970	7,532,812
		12,178,661	10,666,698
Less:			
Expenditure			
Personnel Costs	17	43,037,361	44,005,659
Administration & Establishment Expenses	18	37,326,188	36,062,302
Capital Market Development Expenses	19	18,113,715	6,588,724
IOSCO Conference 2005		-	1,395,719
Finance Charges	20	144,679	148,567
Infrastructure Development Contribution - Tsunami Fund		-	10,000,000
Total Expenditure		98,621,943	98,200,971
Excess Expenditure over Income		(86,443,282)	(87,534,273)
Transfers from Cess Fund to meet Operational Expenses		91,562,575	92,596,078
Excess/(Deficit) for the year		5,119,293	5,061,805

The Accounting Policies and Notes appearing on pages 44 to 55 form an integral part of the Financial Statements.

Statement of Changes in Reserves

for the year ended 31st December 2006

	Reserves Rs.	Accumulated Fund Rs.	Total Rs.
Balance as at 1st January 2005	2,454,777	(7,582,130)	(5,127,353)
Decrease due to disposal of revalued assets	(722,937)	722,937	-
Net Surplus/(Deficit) for the period		5,061,805	5,061,805
Balance as at 31st December 2005	1,731,840	(1,797,388)	(65,548)
Balance as at 1st January 2006	1,731,840	(1,797,388)	(65,548)
Decrease due to disposal of revalued assets	(1,705,433)	1,705,433	-
Net Surplus/(Deficit) for the period	-	5,119,293	5,119,293
Balance as at 31st December 2006	26,407	5,027,338	5,053,745

The Accounting Policies and Notes appearing on pages 44 to 55 form an integral part of the Financial Statements.

Cash Flow Statement

for the year ended 31st December 2006

	2006 Rs.	2005 Rs.
Cash Flows from Operating Activities		
Net Increase(Decrease) after transfers from Cess Fund	5,119,293	5,061,805
Adjustment for		
Depreciation	1 9,760,309	9,336,509
(Profit)/Loss on Disposal of Property, Plant & Equipment	(1,969,494)	(562,992)
Recognition of Grant	14 (7,884,970)	(7,532,812)
Provision for Gratuity	15 1,223,314	3,238,573
Net Increase(Decrease) before Working Capital Changes	6,248,452	9,541,083
Change of Working Capital		
(Increase)/Decrease of Stocks	95,844	5,534
(Increase)/ Decrease of Receivable	(121,121)	(111,832)
(Increase)/Decrease of Deposits Advances & Prepayments	(807,415)	899,038
Increase/(Decrease) of Receipt in Advance	104,393	114,489
Increase/(Decrease) of Creditors & Accruals	5,315,044	(2,009,531)
	4,586,745	(1,102,302)
Cash generated from Operating Activities	10,835,197	8,438,781
Gratuity paid during the year	(536,223)	(2,046,820)
Net Cash from Operating Activities	10,298,974	6,391,961
Extra Ordinary Items - Life Insurance claim received for an employee	-	5,636,627
Interest earned on the Life Insurance claim placed on Repo investment	180,651	-
	10,479,625	12,028,588
Cash Flows into Investing Activities		
Purchase of Property Plant and Equipment	(6,237,425)	(18,306,054)
Proceeds from sale of Property Plant & Equipment	2,669,496	3,662,812
Net Cash from Investing Activities	(3,567,929)	(14,643,242)
Cash Flows from Financing Activities		
Capital Transfer from Cess Fund	2,437,425	13,006,054
Life Insurance along with interest paid as per the testamentary court order	(5,817,279)	-
Increase (Decrease) in Finance Lease	902,667	2,186,960
Net Cash from Financing Activities	(2,477,187)	15,193,014
Net increase/ (decrease) in Cash and Cash Equivalents	4,434,509	12,578,360
Cash and Cash Equivalents at beginning of period (Note a)	12,679,593	101,233
Cash and Cash Equivalents at end of period (Note b)	17,114,102	12,679,593
Note (a)		
Cash and Cash Equivalents at beginning of period		
Cash at Bank	7,022,966	81,233
Cash in Hand	20,000	20,000
REPO Investments	5,636,627	-
	12,679,593	101,233
Note (b)		
Cash and Cash Equivalents at End of period		
Cash at Bank	17,094,102	7,022,966
Cash in Hand	20,000	20,000
REPO Investments	-	5,636,627
	17,114,102	12,679,593

The Accounting Policies and Notes appearing on pages 44 to 55 form an integral part of the Financial Statements.

CESS Fund

Cash Flow Statement

for the year ended 31st December 2006

	2006 Rs.	2005 Rs.
Cash Flows from Operating Activities		
Net Increase of Cess Fund	157,064,903	140,115,770
Net Increase before working capital changes	157,064,903	140,115,770
Change of Working Capital		
(Increase)/Decrease of Staff Loans	38,674	646,519
(Increase)/Decrease of Receivables	52,349	123,608
(Increase)/Decrease of Interest Receivable on Treasury Bills	(20,639,468)	(25,584,936)
Increase/(Decrease) of Other Payables	60,370	(66,099)
(Increase)/Decrease of Rent Deposit	-	(45,890)
	<u>(20,488,075)</u>	<u>(24,926,798)</u>
Net Cash from Operating Activities	136,576,828	115,188,972
Cash Flows into Investing Activities		
Investment of Treasury Bills	(129,955,473)	(119,114,161)
Net Cash from Investing Activities	(129,955,473)	(119,114,161)
Net Increase/(Decrease) in Cash and Cash Equivalents	6,621,355	(3,925,189)
Cash and Cash Equivalents at beginning of period (Note c)	252,423	4,177,612
Cash and Cash Equivalents at end of period (Note d)	6,873,778	252,423
Note (c)		
Cash and Cash Equivalents at beginning of period		
Cash at Bank	252,423	177,612
REPO Investments	-	4,000,000
	<u>252,423</u>	<u>4,177,612</u>
Note (d)		
Cash and Cash Equivalents at end of period		
Cash at Bank - Placed on Overnight REPO Investments	6,873,778	252,423
	6,873,778	252,423

The Accounting Policies and Notes appearing on pages 44 to 55 form an integral part of the Financial Statements.

Compensation Fund

Cash Flow Statement

for the year ended 31st December 2006

	2006 Rs.	2005 Rs.
Cash Flows from Operating Activities		
Net Increase of Compensation Fund	8,661,008	11,816,434
Net Increase before Working Capital Changes	8,661,008	11,816,434
Change of Working Capital		
(Increase)/Decrease of Interest Receivable on Treasury Bills	(913,318)	(1,709,127)
Increase/(Decrease) of Other Payables	19,696	(10,256)
	<u>(893,622)</u>	<u>(1,719,383)</u>
Net Cash from Operating Activities	7,767,386	10,097,051
Cash Flows into Investing Activities		
Investment in Treasury Bills	(7,740,594)	(10,158,789)
Net cash from investing activities	(7,740,594)	(10,158,789)
Cash Flows from Financing Activities		
Net Increase/(Decrease) in Cash and Cash Equivalents	26,792	(61,738)
Cash and Cash Equivalents at beginning of period (Note e)	65,589	127,327
Cash and Cash Equivalents at end of period (Note f)	<u>92,381</u>	<u>65,589</u>
Note (e)		
Cash and Cash Equivalents at beginning of period		
Cash at Bank	48,229	109,968
Call Deposits	17,360	17,359
	<u>65,589</u>	<u>127,327</u>
Note (f)		
Cash and Cash Equivalents at end of period		
Cash at Bank	76,022	48,229
Call Deposits	16,359	17,360
	<u>92,381</u>	<u>65,589</u>

The Accounting Policies and Notes appearing on pages 44 to 55 form an integral part of the Financial Statements.

Accounting Policies

1. SIGNIFICANT ACCOUNTING POLICIES

1.1 BASIS OF PREPARATION

The Financial Statements of the Commission are presented in Sri Lankan Rupees rounded to the nearest Rupee. The Financial Statements are prepared under the historical cost convention. Where appropriate accounting policies are disclosed in succeeding notes.

1.2 STATEMENT OF COMPLIANCE

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

1.3 EVENTS AFTER THE BALANCE SHEET DATE

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

1.4 COMPARATIVE FIGURES

Comparative figures have been adjusted to conform to the changes in presentation in the current financial year and/or described by a narration.

2. ASSETS & BASES OF VALUATION

2.1 PROPERTY, PLANT AND EQUIPMENT

OWNED PROPERTY PLANT AND EQUIPMENT

Property, Plant & Equipment together with any incidental expenses there on are stated at cost or as per the revaluation and depreciated at their respective useful lives. Fixed assets received as grants, were accounted at cost and depreciation thereof is charged against the respective reserve account. In respect of disposal of revalued assets the balance remaining in the revaluation reserve is charged to the Accumulated Fund. The depreciation is provided on the straight-line basis applying following rates:

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

Full year depreciation is provided for all assets purchased during the first half of the financial year and no depreciation is provided for assets purchased during the second half of the year. In the year of disposal depreciation is provided up to the date of receiving disposal proceeds.

2.2 LEASED MOTOR VEHICLES

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

As part of the remuneration package the managerial staff is entitled to a vehicle under the contributory lease scheme. Whilst the SEC pays the lease rental the staff concerned contributes towards the lease rental. In addition the staff should bear all the expenditure in full pertaining to comprehensive insurance, license and maintenance. The ownership of the vehicle will be transferred to the member of the staff who participated in the contributory lease scheme at the expiration of the lease period i.e. after 48 months or upon settlement of the lease liability by the staff concerned in full.

2.3 INVESTMENTS

Government Treasury bills are stated at cost.

2.4 INVENTORIES

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

2.5 RECEIVABLES

Receivables are stated at the estimated realizable value.

3. LIABILITIES & PROVISIONS

3.1 RETIREMENT BENEFITS

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

3.1.2 DEFINED CONTRIBUTION PLANS

All permanent employees' are eligible for Employees' Provident Fund Contributions and Employees' Trust Fund Contributions in line with the respective statutes and regulations. The Commission contributes 12% and 3% of gross emoluments of employees to Employees' Provident Fund and Employees' Trust Fund respectively.

3.2 ACCOUNTS PAYABLE

Payables are stated at cost.

3.3 GRANT

Capital Expenditure transferred from the Cess Fund is treated as a grant and recognized on the estimated useful life of the asset.

4. INCOME & EXPENDITURE

4.1 REVENUE RECOGNITION

Revenue is recognized on accrual basis.

4.2 EXPENDITURE RECOGNITION

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

4.3 CASH FLOW STATEMENT

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

Notes to the Financial Statement

1. Property, Plant & Equipment

COST	Motor Vehicles	Furniture, Fixtures & Fittings	Office Equipment (EDP & Others)	Training Equipment	Assets on		Total
					Finance Lease	Motor Vehicles	
Balance as at 1st January 2006	17,255,900	4,328,132	16,939,106	1,836,400	10,900,000		51,259,538
Additions during the Year	-	77,736	2,178,107	181,582	3,800,000		6,237,425
Disposals during the year	(1,200,000)	(3,466)	(747,442)	-	(4,200,000)		(6,150,908)
Balance as at 31st December 2006	16,055,900	4,402,402	18,369,771	2,017,982	10,500,000		51,346,055
ACCUMULATED DEPRECIATION							
Balance as at 1st January 2006	7,701,475	2,214,849	11,573,825	1,550,650	4,125,000		27,165,799
Depreciation Charge for the Year	3,801,475	527,425	2,822,444	233,965	2,375,000		9,760,309
Accumulated Depreciation On Disposal of Assets	(1,200,000)	(3,467)	(747,439)	-	(3,500,000)		(5,450,906)
Balance as at 31st December 2006	10,302,950	2,738,807	13,648,830	1,784,615	3,000,000		31,475,202
WRITTEN DOWN VALUE AS AT 31ST DECEMBER 2006	5,752,950	1,663,595	4,720,941	233,367	7,500,000		19,870,853
WRITTEN DOWN VALUE AS AT 31ST DECEMBER 2005	9,554,425	2,113,283	5,365,281	285,750	6,775,000		24,093,739

2. CESS INVESTMENT AND OTHERS	2006 Rs.	2005 Rs.
NON CURRENT ASSETS		
Staff Loans	2,957,441	3,267,365
Rent Deposits	4,825,032	4,825,032
	<u>7,782,473</u>	<u>8,092,397</u>
Invested in State Institutions-Temporary Surplus Fund	300,000,000	-
Investment in Treasury Bills	404,972,749	575,017,276
	<u>704,972,749</u>	<u>575,017,276</u>
CURRENT ASSETS		
Staff Loans receivable within 12 months	1,647,850	1,376,600
Withholding Tax Receivables	400,341	400,341
Interest Receivable on Treasury Bills	52,315,238	31,675,770
Cess Receivables	1,727,132	1,779,481
Balance at Bank - Placed on Overnight Repo Investment	6,873,778	252,423
	<u>62,964,339</u>	<u>35,484,615</u>
Total Assets	<u>775,719,561</u>	<u>618,594,288</u>
LIABILITIES		
Custodian Fees Payable	60,370	-
	<u>775,659,191</u>	<u>618,594,288</u>
3. COMPENSATION INVESTMENT AND OTHERS		
ASSETS		
Investment in Treasury Bills	54,305,516	46,564,922
CURRENT ASSETS		
Withholding Tax Receivable on Call Deposit	72,445	72,445
Interest Receivable on Treasury Bills	3,669,451	2,756,133
Investment in Call Deposits	16,359	17,360
Balance at Bank	76,022	48,229
	<u>3,834,277</u>	<u>2,894,167</u>
Total Assets	<u>58,139,793</u>	<u>49,459,089</u>
LIABILITIES		
Custodian Fees Payable	19,696	-
	<u>58,120,097</u>	<u>49,459,089</u>
4. INVENTORIES		
Stock of Stationery & EDP Consumables	301,885	399,408
Stock of Publications	3,059	1,380
	<u>304,944</u>	<u>400,788</u>
5. RECEIVABLES		
Sundry Debtors Including Debit Notes	269,888	257,035
Withholding Tax Receivable	5,399	5,399
Staff Recoveries	238,420	144,651
Festival Advances	462,000	447,500
	<u>975,707</u>	<u>854,585</u>

	2006 Rs.	2005 Rs.
6. DEPOSITS, ADVANCES & PRE-PAYMENTS		
Safe Vault Deposit - Bank of Ceylon	20,000	20,000
Deposit for Cellular Phones	80,000	40,000
Fuel Deposit	35,000	55,000
Deposit for Vehicle Maintenance	500	500
Deposits with Sri Lanka Telecom Ltd	42,125	42,125
Hot & Cold Dispenser	8,000	213,799
Advances to Suppliers	1,011,972	562,511
Registration Fees - Foreign Training	543,753	-
	1,741,350	933,935
7. LIFE INSURANCE PAYABLE		
Balance at the beginning of the period	5,636,627	-
Add: Interest earned on REPO investments	180,651	-
Less: Payment made as per the Court order	(5,817,278)	5,636,627
	-	5,636,627
<p>(The life insurance claim received on account of a former employee was invested in a Repo account until the life insurer's testamentary case was over and settled along with the interest earned on Repo investment in accordance with the Court order during the year under review).</p>		
8. CASH		
Cash at Bank	17,094,102	7,022,966
Cash in Hand	20,000	20,000
	17,114,102	7,042,966
9. RESERVES		
REVALUATION SURPLUS		
Balance at the beginning of the period	1,731,840	2,454,777
Less: Disposal of Assets	(1,705,433)	(722,937)
Balance at the end of the period	26,407	1,731,840
10. ACCUMULATED FUND		
Balance at the beginning of the period	(1,797,388)	(7,582,130)
Add Decrease due to the revaluation	1,705,433	722,937
Net Surplus/(Deficit) for the period	5,119,293	5,061,805
Balance at the end of the period	5,027,338	(1,797,388)
11. CESS FUND		
Opening Balance	618,594,288	478,478,518
Add: Cess Received during the year	185,014,391	206,276,152
Interest on Investment	66,316,820	39,732,085
	869,925,499	724,486,755
Less: Transfers to Operational & Capital Expenditure	94,000,000	105,602,132
Expenses	1,700	22,900
Custodian Fees	264,608	267,435
	94,266,308	105,892,467
Closing Balance	775,659,191	618,594,288

12. COMPENSATION FUND	2006	2005
	Rs.	Rs.
Opening Balance	49,459,089	37,642,655
Compounding fees received during the year	3,850,000	8,650,000
Add : Interest on Investment - Treasury Bills	4,866,953	3,197,798
	58,176,042	49,490,453
Less: Custodian Fees	40,603	21,904
Bank Charges	15,342	9,460
	55,945	31,364
Closing Balance	58,120,097	49,459,089
13. LEASE CREDITOR		
Gross Lease Liabilities	9,713,220	8,505,881
Interest in Suspense	(1,881,087)	(1,576,415)
	7,832,133	6,929,466
Less: Payable within one year	(2,471,892)	(2,362,553)
Payable after one year	5,360,241	4,566,913
14. GRANT - CAPITAL TRANSFERS FROM CESS FUND		
Balance Brought Forward	18,269,284	12,796,042
Transfers During the Year	2,437,425	13,006,054
Less: Transferred to Income for Assets Depreciation	(7,884,970)	(7,532,812)
	12,821,739	18,269,284
RECOGNITION OF GRANT		
Capital Transfers from Cess Fund	7,884,970	7,532,812
	7,884,970	7,532,812
Note		
Recognition of Grant		
Capital Transfers from Cess Fund		
Recognition of Grant in accordance with the SLAS 24 at the following rates.		
Motor Vehicles	25.00%	25.00%
Office Equipment - Others & EDP	25.00%	25.00%
Training Equipment	25.00%	25.00%
Furniture, Fixtures & Fittings	12.50%	12.50%
15. RETIREMENT BENEFIT OBLIGATION		
Balance Brought Forward	5,161,801	3,970,048
Charge for the Year	1,223,314	3,238,573
Gratuity Paid During the Year	(536,223)	(2,046,820)
	5,848,892	5,161,801

	2006 Rs.	2005 Rs.
16. CREDITORS AND ACCRUALS		
Telephone Expenses	167,960	198,854
Electricity	80,768	49,075
Fuel Expenses	33,292	43,568
Staff Medical Reimbursements	200,000	144,627
Staff Welfare	179,084	25,765
Staff Training Local	122,117	-
Leave Encashment	237,656	207,165
Interest Subsidy	4,424	-
Security Charges	27,900	-
Office Upkeep	13,031	-
Overtime	51,096	-
Foreign Travel	123,036	-
External Audit Fees	350,000	150,000
Internal Audit Fees	150,000	-
Printing of the Annual Report	1,251,471	1,500,000
Newspapers & Periodicals	5,675	4,755
VAT Payable	24,365	106,743
Other Payables	15,265	67,256
Members Fees	6,000	-
Courier Charges	5,000	-
Professional Charges	166,395	-
Document Scanning	581,790	-
Developmental Assistance Internet Trading	4,140,000	-
IOSCO Payable	-	123,473
	7,936,325	2,621,281
17. PERSONNEL COSTS		
Staff Salaries	21,965,040	20,767,373
Chairman's Allowance	328,052	337,956
Overtime	727,334	573,134
E P F & E T F	3,374,638	3,107,671
Staff Medical Expenses & Insurance	1,371,615	1,777,035
Annual Bonus/Ex-Gratia payment	1,901,260	412,873
Staff Gratuity	1,223,315	3,238,573
Leave Encashment	332,298	526,382
Compensation	158,061	119,962
Staff Housing Loan Interest Subsidy	355,812	419,577
Staff Welfare	1,046,907	744,313
Staff Travelling Allowance	-	73,800
Reimbursement of Fuel - Directors	821,706	672,610
Foreign Travel & Training - Staff	6,089,293	4,631,265
Foreign Travel - Commission Members	1,862,740	4,243,416
Staff Training - Local	996,397	911,239
Temporary Allowance paid for IBSL work	380,429	1,384,154
Interns Allowance	102,464	64,326
	43,037,361	44,005,659

18. ADMINISTRATION & ESTABLISHMENT EXPENSES	2006 Rs.	2005 Rs.
Rent & Car Park Rental	10,242,460	10,986,373
Electricity Charges	973,354	1,308,145
Office Upkeep	234,921	156,178
Security Chargers	280,920	257,370
Office Equipment maintenance & Insurance	607,821	534,310
Telephone, Internet, E- mail & Web	2,089,943	2,736,203
Motor Vehicle Maintenance & Insurance	915,561	873,895
Legal Expenses	442,529	371,375
Professional Fees	2,006,220	2,185,498
Member Fees	71,000	118,000
Meeting Expenses	177,158	113,154
Entertainment	271,658	221,281
International Membership Fees - IOSCO	1,259,036	1,083,938
Depreciation	9,760,309	9,336,509
Cost of Publications	9,588	16,450
Obsolete stocks	38,300	125,668
Advertising	982,926	256,300
Market Surveillance Cost	1,183,652	1,144,841
Library Books	146,900	88,906
Printing & Stationery	1,150,937	2,304,678
Travelling-Local	92,034	88,477
Insurance Fire & Personal Accident	268,669	272,598
News Papers & Periodicals	107,649	64,374
Postage	41,884	46,145
Courier Charges	75,077	167,182
Audit Fees -Internal	301,913	96,060
Audit Fees -External	200,000	150,000
General Expenses	50,476	37,426
Trade Tax	5,000	5,000
Vat Expenses	2,757,671	374,970
Lease Finance Charges	580,622	540,998
	37,326,188	36,062,302

* The input VAT that cannot be set off against the output VAT is reflected as VAT expenses unlike in the previous years where the amount unclaimed was reflected against the item of expenditure.

19. CAPITAL MARKET DEVELOPMENT

Capital Market Development - CSE Kurunagala/Kandy Branch	2,880,000	1,000,000
Developmental Assistant - Internet Trading	7,371,187	-
Public Awareness Programmes	7,862,528	5,588,724
	18,113,715	6,588,724

20. IOSCO CONFERENCE 2005	2006 Rs.	2005 Rs.
Income		
Registration Fee		23,482,648
Accomodation Fee		19,111,665
Accompanying Persons Fee		2,125,717
Tours		932,183
Exhibition Booths		1,308,942
Interest earned		127,112
Total Income	-	47,088,267
Less		
Expenditure		
IOSCO Hosting Fee		15,567,952
Hotel Accomodation		10,824,658
BMICH		4,193,694
Conference Planning, Admn. & Organising Fee		3,252,230
Transport		352,461
Interpreters, Translators, & Panelist		2,662,385
Information Technology & Telecommunication		1,022,999
Stationery		1,806,454
Interior Decorations		142,100
Complimentary Items		716,755
Entertainment		3,600,646
Welfare		949,349
Advertising		746,568
Miscellaneous		260,820
Human Resources		1,382,340
IOSCO Foreign Travel		287,591
Bank Charges		660,546
Exchange Loss		54,438
Total Expenditure	-	48,483,986
Expenditure Over Income	-	1,395,719

The following organisations sponsored lunches/dinners for the participants of IOSCO Conference 2005 amounting to Rs. 10 Million. The respective organisations settled the hotel bills directly.

Colombo Stock Exchange	3 Million
Millenium IT	3 Million
Stock Brokers Association of Sri Lanka	1.3 Million
Insurance Association of Sri Lanka	2.7 Million

21. FINANCE CHARGES

Bank Charges	54,209	56,800
Debit Tax	90,470	91,767
	144,679	148,567

22. TAXATION

The Commission is not liable for income tax in terms of the Inland Revenue Act No. 28 of 1979 as amended by Act No. 38 of 2000.

23. CAPITAL COMMITMENTS

There were no capital commitments as at 31st December 2006 except to award the bid pertaining to interior designing including refurbishing of two new floors to relocate the SEC at the World Trade Center costing approximately Rs 16,520,000/-.

24. CONTINGENT LIABILITIES

There were no contingent liabilities as at 31st December 2006.

25. EVENTS AFTER THE BALANCE SHEET DATE

No material events have occurred after the Balance Sheet date necessitating any adjustments or disclosure in the Financial Statements.

26. RELATED PARTY DISCLOSURES

Mr Gamini Wickramasinghe was appointed to the post of Chairman of the SEC on 3rd February 2006.

The following Members of the Commission assumed office as stated below.

Ex officio Members re-appointed

Mr D K Hettiarachchi	w.e.f	13 th March 2006
Dr Mrs Rane Jayamaha	w.e.f	22 nd February 2006
Mr S Abeysinghe	w.e.f	22 nd February 2006
Mr Yohan Perera	w.e.f	22 nd March 2006

Newly appointed Members

Mr C P E Gunasingam	w.e.f	3 rd February 2006
Mr Graetian Gunawardhana	w.e.f	3 rd February 2006
Mrs Siromi N Wickramasinghe	w.e.f	27 th March 2006

Notes to the Financial Statement Contd...

The following table depicts the relationships held by the Members of the Commission as at end of the year.

Name	Name of related Institution	Relationship
Mr G Wickramasinghe	Informatics (Pvt) Ltd	Director
	Informatics Institute of Technology Ltd	Director
	Informatics Information Systems (Pvt) Ltd	Director
	Informatics Agrotech (Pvt) Ltd	Director
	Visual Computing Systems (Pvt) Ltd	Director
	Informatics International Ltd	Director
	Informatics Hospitality Systems Ltd	Director
	Informatics International Lanka (Pvt) Ltd	Director
	Informatics Holdings Ltd	Director
	Charles Exports (Pvt) Ltd	Director (w.e.f 8 th June 2006)
	Industrial and Financial Systems Solutions Ltd	Director
	Systems Integrators (Private) Ltd	Director
	Informatics Trading (Private) Ltd	Director
	Industrial and Financial Systems Sri Lanka Ltd	Director
	Insurance Board of Sri Lanka	Chairman (w.e.f 3 rd February 2006)
Settlement Guarantee Fund	Trustee (w.e.f 3 rd February 2006)	
Mr D K Hettiarachchi	Sri Lanka Accounting Standard Monitoring Board	Member
Dr (Mrs) Ranee Jayamaha	Insurance Board of Sri Lanka	Ex officio Member
	Credit Information Bureau	Chairperson
	National Council for Economic Development – Financial Sector Cluster	Co-Chairperson
	National Payments Council	Chairperson (from March 2006)
	Technical Committee on Regulation of Share Ownership in Banks	Chairperson (from October 2006)
Mr S Abeysinghe	Bank of Ceylon	Director (Treasury Nominee)
	Insurance Board of Sri Lanka	Member (Treasury Nominee)
	Settlement Guarantee Fund	Trustee
	De-La Rue Lanka	Director (Treasury Nominee)
	President Fund	Member of the Board
Mr Yohan Perera	Postgraduate Institute of Management (PIM)	Member, Board of Management
	National Institute of Business Management (NIBM)	Member, Governing Council
	KPMG Ford, Rhodes, Thornton & Co. Chartered Accountants	Partner
	FRT Holdings (Private) Ltd.	Director
	Industrial & Commercial Consultants Ltd.	Director
	E Business Exchange Lanka (Private) Ltd.	Director
Mr C P E Gunasigham	Jaguar (Pvt) Ltd	Director
	Insurance Board of Sri Lanka	Member of the Board (w.e.f 3 rd February 2006)
Mr Graetian Gunawardhana	National Development Health Fund	Member of the Board of Trustee
	Insurance Board of Sri Lanka	Member of the Board (3 rd February 2006)
	Hands International (Pvt) Ltd	Chairman / Managing Director
Mrs Siromi Wickramasinghe	-	-

The following Members of the SEC were also Members of the Insurance Board of Sri Lanka (IBSL) during the year under review except Mr Channa de Silva who is the Director General of the SEC.

Mr Gamini Wickramasinghe	Chairman IBSL
Dr Mrs Rane Jayamaha	Member of the Board
Mr S Abeysinghe	Member of the Board
Mr C P E Gunasingam	Member of the Board
Mr Graetian Gunawardhana	Member of the Board
Mr Channa de Silva	Member of the Board

The Commission received the following amounts from the IBSL for goods and services provided during the year under review at cost:

	Rs.
Remuneration for seconding staff from SEC to IBSL	1,407,400.25
Management Fee	392,000.00
Office equipment maintenance	12,282.00
Vehicle hire	61,030.00
Stationaries	27,459.50
Car Parking	112,000.00
Meeting Expenses	1,800.00
Total	2,013,971.75

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

Report of the Auditor General



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මගේ අංකය. }
எனது இல. } LP/F/SEC/2007/01
My No. }

ඔබේ අංකය. }
உமது இல. }
Your No. }

දිනය. }
திகதி. } 09th July 2007
Date. }

The Chairman,
Securities and Exchange Commission of Sri Lanka

Report of the Auditor General on the Financial Statements of the Securities and Exchange Commission of Sri Lanka for the year ended 31 December 2006 in terms of Section 14(2)(c) of the finance Act No. 38 of 1971.

The audit of financial statements of the Securities and Exchange Commission of Sri Lanka (SEC) for the year ended 31 December 2006 was carried out under my direction in pursuance of provisions in Article 154(1) of the Constitution of the Democratic Socialist Republic of Sri Lanka read in conjunction with Section 13(1) of the Finance Act No. 38 of 1971 and Section 37(2) of the Securities and Exchange Commission Act No. 36 of 1987. My observations which I consider should be published with the annual report of the Commission in terms of Section 14(2)(c) of the Finance Act appear in this report. A detailed report in terms of Section 13(7)(a) of the Finance Act will be furnished to the Chairman of the Commission in due course.

1:2 Scope of Audit

Audit opinion, comments and findings in this report are based on a review of the financial statements presented to audit and substantive test of samples of transactions. The scope and the extent of such review and tests were such as to enable as wide an audit coverage as possible within the limitation of staff, other resources and time available to me. The audit was carried out in accordance with Sri Lanka Auditing Standards, methods and practices to obtain reasonable assurance as to whether the financial statements are free of material misstatements. The audit included examination of evidence supporting the amounts and disclosures in financial statements and assessment of accounting principles and significant estimates and judgements made in the preparation of financial statements, evaluation of their overall presentation and determining whether accounting policies adopted were appropriate, consistently applied and adequately disclosed. Sub-sections (3) and (4) of Section 13 of the Finance Act No. 38 of 1971 give discretionary powers to the Auditor General to determine the scope and extent of the audit.

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කොළඹ 07, ශ්‍රී ලංකාව.

சுதந்திர சதுக்கம்,
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2. Accounts

2:1 Opinion

So far appears from my examination and to the best of my information and according to the explanations given to me, I am of opinion that the Securities and Exchange Commission of Sri Lanka had maintained proper books of account for the year ended 31 December 2006 and the financial statements which are in agreement with the said books have been prepared and presented in accordance with Sri Lanka Accounting Standards and the stated accounting policies and notes (Nos. 01 to 26) to the financial statements give a true and fair view of the financial position of the Securities and Exchange Commission of Sri Lanka as at 31 December 2006, and the results of its operations and cash flow for the year then ended.

3. Financial and Operating Review

3:1 Financial Results

According to the financial statements presented, the operations of the Commission for the year ended 31 December 2006 had resulted in a net deficit of Rs. 86,443,282 before taking into account the transfers from Cess Fund for operational expenses as compared with the corresponding net deficit of Rs. 87,534,273 before taking into account the transfers from Cess Fund for the preceding year. The operating surplus for the year under review after taking into accounts the transfers from the Cess Fund for operational expenses for the year amounted to Rs. 5,119,293 as compared with the corresponding net surplus of Rs. 5,061,805 in the preceding year after taking into accounts the transfers from the Cess Fund for that year.

3:2 Idle and Under - utilized Assets

The Access Control System installed in the office premises of the Commission by spending a sum of Rs. 690,862 had been abandoned at the end of the year 2004 as the Commission had an opinion that it did not serve any useful purpose. However, this system remaining in the office premises without being disposed off.

3:3 Investment in Surplus Funds

The Commission had deposited a sum of Rs. 300,000,000 in the State Institutions Temporary Surplus Trust Fund in terms of the Public Enterprises Circulars No. 30 of 13 July 2005 and No. PED 33 of 19 December 2005. However, action had not been taken to transfer the investments of Cess Fund and Compensation Fund held in Treasury Bills amounting to Rs. 459,278,265 as at 31 December 2006 to the above funds as requested by the same Circulars.

3:4 Performance of the Commission

Following observations are made.

- (i) It was observed that the Commission had failed to reach the expected level of performance by achieving some of the main goals, which were included in the Corporate Plan.
Details are as follows.
 - (a) The Commission has expected to encourage and facilitate the increase of new listing of companies in the stock market by 30% in order to improve the overall economy of the Country. However, only two companies were listed while four others were delisted in the year 2006. Hence, listing of companies decreased by 0.8% in the year under review.

- (b) Another goal of the Commission was to increase the Market Capitalization to 50% of the Gross Domestic Product (GDP) by end of 2006. However, Market Capitalization for the year 2006 was Rs. 834.76 Billion and it represented only 34.16% of the GDP (Rs. 2443.53 Billion), which was based on the actual figures up to end of 08 September 2006.
- (c) It had been planned to increase the Annual Turnover in the Equity Market by 50% annually. However, Annual Turnover of the Equity Market in 2006 was Rs. 105,153 Million and it shows a decrease of 8.2% when compared with that of the previous year. Accordingly, the target seems to be unrealistic.

The Director General of the Commission informed me as follows.

“These indicative targets were fixed at a time when the scenario pertaining to the securities market was very promising. However market conditions changed, which were beyond the control of the Secretariat. Despite the changes in the market conditions the results achieved during year 2006 was extremely satisfactory”.

- (ii) Following activities included in the Action plan for the year 2006 had not been completed.
 - (a) Strengthen the procedures for obtaining advice from the Sri Lanka Accounting and Auditing Standards Monitoring Board on matters pertaining to Listed Companies.
 - (b) Streamline complaints and Investigation Process
 - (c) Formulate a procedure to send notice/letters to the brokers, investment advisers, as well as investors, upon detection of specific violation after the Surveillance Committee determination.
 - (d) Finalization of revision of Takeovers and Mergers Code
 - (e) Finalization of Securitisation Law
 - (f) Finalization of revision of member Regulations
 - (g) Facilitation of a time bound plan to focus on the investigation at each stage
 - (h) Formulate Reporting Formats for Market Intermediaries
 - (i) Develop benchmarks and Ratio Analysis to analyse Market Intermediaries, Stock brokers and Stock Dealers
 - (j) Train staff on 5s (five step method of organizing the work place) and implementation of 5s
 - (k) Process study for an on line reporting system for market intermediaries, stock brokers and listed companies
 - (l) Form a Committee on investment policy and document guidelines.

The Director General of the Commission informed me as follows.

“As mentioned some of the activities fell short of the plan in some instances due to the intricacies that arose whilst formulating legislation that needs careful deliberations prior to finalizing same. Some of the above mentioned activities have been incorporated to the Corporate Plan of year 2007 and currently the work is in progress. However substantial work was carried out during the year 2006 whilst laying a strong foundation to create a vibrant Capital Market in Sri Lanka”.

One of the core functions of the Corporate Affairs Division of the Commission is to monitor the timely submission of reports and compliance of listed companies with Sri Lanka Accounting Standards, Companies Act, Stock Exchange Rules and SEC Act. However, out of 237 listed companies Annual Reports of 7 listed companies were reviewed by the SEC during the year 2006 and this activity has not been functioned in last two years at all. As the regulator of the capital market, SEC has the responsibility to protect the rights of investors from fraudulent activities of listed companies. Since SEC has failed to assure the reliability of information provided by the annual reports during the last three years, it was observed that they have neglected their responsibility.

The Director General of the Commission informed me as follows.

"As you are aware the SEC mandate became much wider with the amendments carried out to the SEC Act in the year 2003. At that stage the Secretariat discontinued reviewing the Annual reports of listed companies since the Secretariat wanted to concentrate more on regulating the new Market Intermediaries.

In terms of Section 23 of the Sri Lanka Accounting and auditing Standards Act No. 15 of 1995 "The function of the board shall be to monitor the compliance with the Sri Lanka Accounting Standards, and Sri Lanka Auditing Standards, by specified business enterprises".

Subsequently the Secretariat felt with the growth of the Market that it was necessary to have a close review of the Annual Reports with a view to identify and rectify non-compliance with rule 8.6 of the Stock Exchange Listing Rules expeditiously.

Therefore it was decided to reintroduce the review of accounts and increase the staff strength to support this initiative. On an overall basis 2006 was a year that SEC engaged in many substantial market development initiatives whilst strengthening the regulatory framework".

4. Follow up action to the directions given by the COPE meeting

Following matters were observed relating to the direction given at the meeting of the Committee on Public Enterprises held on 11 January 2007.

- (a) Only one member, out of two vacancies of the members of the Commission had been appointed. The Secretariat has also recommended names of a few suitable candidates to the ministry of Finance and planning in order to fill the other vacancy.
- (b) The report with regard to cross listing of shares and its impact to the economy of Sri Lanka as requested by the committee had been submitted after 2 month from the due date.
- (c) Since the Commission did not receive any suitable candidates for the position of Deputy Director General, the appointment had been deferred. Therefore action had not been taken to submit a detailed report within two weeks as requested by the Committee.



P. A. PEMATILAKA
AUDITOR GENERAL

Responses of the SEC to the matters raised by the Auditor General

Auditor General's Observations	SEC responses
<p>3.2 Idle and under utilized assets</p> <p>The Access Control System installed in the office premises of the Commission spending a sum of Rs 690,862 had been abandoned at the end of the year 2004 as the Commission had an opinion that it did not serve any useful purpose. However, this system remaining in the office premises without being disposed of.</p>	<p>The CCTV cameras of the Access Control System are used for the security purposes of the Commission and agree that the access control is not used.</p>
<p>3.3 Investment in surplus fund</p> <p>The Commission had deposited a sum of Rs 300,000,000/- to the State Institutions Temporary Surplus Trust Fund in terms of the Public Enterprise Circular No 30 of 13th July 2005 and No PED 33 of 19 December 2005. However action had not been taken to transfer the investments of Cess Fund and Compensation Fund held in Treasury Bills amounting to Rs 459,278,265 as at 31 December 2006 to the above funds as requested by the same Circulars.</p>	<p>The Commission at its 209th meeting held on 24th February 2006 decided to transfer a sum of Rs 300mn based on the balance lying to the credit of the Cess Fund then. Steps will be taken to ascertain and transfer the surplus money upon finalizing the Audit for the year 2006.</p>
<p>3.4 Performance of the Commission</p> <p>Following observations are made.</p> <p>(l) It was observed that the Commission has failed to reach the expected level of performance by achieving some of the main goals, which were included in the Corporate Plan. Details are as follows;</p> <p>(a) The Commission has expected to encourage and facilitate the increase of new listing of companies in the stock market by 30% in order to improve the overall economy of the country. However, only two companies were listed while four others were de-listed in the year 2006. Hence listings of companies decreased by 0.8% in the year under review.</p> <p>(b) Another goal of the Commission was to increase the Market Capitalization to 50% of the Gross Domestic Product (GDP) by end of 2006. However Market capitalization for the year 2006 was Rs. 834.76 Billion and it represents only 34.16% of the GDP (Rs 2,443.53 Billion), which was based on the actual figures up to end of 8th September 2006.</p> <p>(c) It had been planned to increase the Annual Turnover in Equity Market by 50% annually. However, Annual Turnover of the Equity Market in 2006 was Rs 105,153 Million and it shows a decrease of 8.2% when compared with that of the previous year. Accordingly, target fixed seems to be unrealistic.</p>	<p>These indicative targets were fixed at a time when the scenario pertaining to the securities market was very promising. However market conditions changed, which were beyond the control of the Secretariat. Despite the changes in the market conditions the results achieved during year 2006 was extremely satisfactory.</p>

<p>The Director General of the Commission informed me as follows.</p> <p>“These indicative targets were fixed at a time when the scenario pertaining to the securities market was very promising. However market conditions changed, which were beyond the control of the Secretariat. Despite the changes in the market conditions the results achieved during year 2006 was extremely satisfactory”.</p> <p>(II) Following activities included in the Action Plan for the year 2006 had not been completed.</p> <p>(i) Strengthen the procedures for obtaining advice from the Sri Lanka Accounting and Auditing Standards Monitoring Board on matters pertaining to Listed Companies.</p> <p>(ii) Streamline complaints and Investigation Process.</p> <p>(iii) Formulate a procedure to send notice/letter to the brokers, investment advisers, as well as investors, upon detection of specific violation after the Surveillance Committee determination.</p> <p>(iv) Finalization of revision of Takeovers and Mergers Code</p> <p>(v) Finalisation of Securitisation Law</p> <p>(v) Finalisation of revision of Member Regulations</p> <p>(vii) Facilitation of a time bound plan to focus on the investigation at each stage</p> <p>(viii) Formulate Reporting Formats for Market Intermediaries</p> <p>(ix) Develop benchmarks and Ratio Analysis to analyze Market Intermediaries, Stock brokers and Stock Dealers</p> <p>(x) Train staff on 5S(five step method of organizing the work place) and implementation of 5s.</p> <p>(xi) Process study for an online reporting system for market intermediaries, stock brokers and listed companies</p> <p>(xii) Form a Committee on investment policy and document guidelines.</p> <p>The Director General of the Commission informed me as follows.</p> <p>“As mentioned some of the activities fell short of the Plan in some instances due to the intricacies that arose whilst formulating legislation that needs careful deliberations prior to finalizing same.</p>	<p>As mentioned some of the activities fell short of the Plan in some instances due to the intricacies that arose whilst formulating legislation that needs careful deliberations prior to finalizing same. Some of the above mentioned activities have been incorporated to the Corporate Plan of year 2007 and currently the work is in progress.</p> <p>However substantial work was carried out during the year 2006 whilst laying a strong foundation to create a vibrant Capital Market in Sri Lanka.</p> <p>In this regard significant work carried out during the year 2006 were as follows.</p> <ul style="list-style-type: none"> • Formulated and Developed a 10 year Capital Market Master Plan for the first time in Sri Lanka. • Formulation of rules for Corporate Governance for all listed companies in the areas of Non Executive Directors, Independent Directors, Remuneration Committee, Audit Committee and other disclosures to be implemented on a mandatory basis. • Completed Rules for Market Intermediaries under the categories of Investment Managers, Margin Providers, Underwriters and Credit Rating Agencies. • Processing and granting of licenses to 5 Stockbrokers/ Stock dealers and renewal of licenses to 15 stockbrokers. • Finalized the regulation for Close Ended Unit Trusts. • Concluded investigations and filed action on Market Manipulations and Insider Dealing. • Facilitated capacity to support enforcement of requirements in Anti-Money Laundering legislation. • Implemented documentation archiving from the inception of the SEC. • Recruitments were carried out to strengthen the SEC. • Finalizing plans to launch the Financial Services Academy. <p>In addition to the above the routine regulatory functions were carried out only by a staff of 48 that served the SEC as at the end of the year 2006.</p>
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Responses of the Commission to the matters raised
by the Auditor General Contd...

<p>Some of the above mentioned activities have been incorporated to the Corporate Plan of year 2007 and currently the work is in progress. However substantial work was carried out during the year 2006 whilst laying a strong foundation to create a vibrant Capital Market in Sri Lanka.”</p>	
<p>(III) One of the core functions of the Corporate Affairs Division of the Commission is to monitor the timely submission of reports and compliance of listed companies with Sri Lanka Accounting Standards, Companies Act, Stock Exchange Rules and SEC Act. However out of 237 listed companies Annual Reports of 7 listed companies were reviewed by the SEC during the year 2006 and this activity has not been functioned in last two years at all.</p> <p>As the regulator of the capital market, SEC has the responsibility to protect the rights of investors from fraudulent activities of listed companies. Since SEC has been failed to assure the reliability of information provided by the annual reports during the last three years, it was observed that they have neglected their responsibility.</p> <p>The Director General of the Commission informed me as follows.</p> <p>“As you are aware the SEC mandate became much wider with the amendments carried out to the SEC Act in the year 2003. At that stage the Secretariat discontinued reviewing the Annual reports of listed companies since the Secretariat wanted to concentrate more on regulating the new Market Intermediaries.</p> <p>In terms of Section 23 of the Sri Lanka Accounting and Auditing Standards Act No. 15 of 1995 “The function of the Board shall be to monitor the compliance with the Sri Lanka Accounting Standards, and Sri Lanka Auditing Standards, by specified business enterprises”.</p> <p>Subsequently the Secretariat felt with the growth of the Market that it was necessary to have a close review of the Annual Reports with a view to identify and rectify non-compliance with rule 8.6 of the Stock Exchange Listing Rules expeditiously.</p> <p>Therefore it was decided to reintroduce the review of accounts and increase the staff strength to support this initiative. On an overall basis 2006 was a year that SEC engaged in many substantial market development initiatives whilst strengthening the regulatory framework.”</p>	<p>As you are aware the SEC mandate became much wider with the amendments carried out to the SEC Act in the year 2003. At that stage the Secretariat discontinued reviewing the Annual reports of listed companies since the Secretariat wanted to concentrate more on regulating the new Market Intermediaries.</p> <p>In terms of Section 23 of the Sri Lanka Accounting and Auditing Standards Act No. 15 of 1995 “The function of the Board shall be to monitor the compliance with the Sri Lanka Accounting Standards, and Sri Lanka Auditing Standards, by specified business enterprises.”</p> <p>Subsequently the Secretariat felt with the growth of the Market that it was necessary to have a close review of the Annual Reports with a view to identify and rectify non-compliance with rule 8.6 of the Stock Exchange Listing Rules expeditiously.</p> <p>Therefore it was decided to reintroduce the review of accounts and increase the staff strength to support this initiative. On an overall basis 2006 was a year that SEC engaged in many substantial market development initiatives whilst strengthening the regulatory framework.</p>

Responses of the Commission to the matters raised
by the Auditor General Contd...

<p>4. Follow up action to the direction given by the COPE meeting</p> <p>Following matters were observed relating to the direction given at the meeting of the Committee on Public Enterprises held on 11th January 2007.</p> <p>a) Only one member, out of two vacancies of the members of the Commission had been appointed. The Secretariat has also recommended names of a few suitable candidates to the Ministry of Finance and Planning in order to fill the other vacancy.</p> <p>b) The report with regard to cross listing of shares and its import to the economy of Sri Lanka as requested by the committee had been submitted after 2 month from the due date.</p> <p>c) Since the Commission did not receive any suitable candidates for the position of Deputy Director General the initiative had been deferred. Therefore action had not been taken to submit a detailed report within two weeks as requested by the Committee.</p>	<p>This has been brought to the notice of Ministry of Finance & Planning.</p> <p>SEC engaged in a meaningful and a serious study on the subject as it entails significant degree of brainstorming and policy discussion.</p> <p>Committee required a report only if an appointment was made but no such appointment was made to the post of Deputy Director General.</p>
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Settlement Guarantee Fund

Balance Sheet

as at 31st December 2006

	NOTES	2006 Rs.	2005 Rs.
ASSETS			
CURRENT ASSETS			
Investment in Treasury Bills		112,697,178	104,763,278
Receivables	2	10,088,582	6,955,364
Cash at Bank		35,325	15,602
TOTAL ASSETS		122,821,085	111,734,244
RESERVES AND LIABILITIES			
RESERVES			
Capital Grants - Treasury		50,000,000	50,000,000
Accumulated Fund		72,663,340	61,593,603
		122,663,340	111,593,603
CURRENT LIABILITIES			
Payables	3	157,745	140,641
		157,745	140,641
TOTAL NET ASSETS & LIABILITIES		122,821,085	111,734,244

The notes appearing on pages 68 to 71 form an integral part of the Financial Statements.

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

FOR AND ON BEHALF OF SETTLEMENT GUARANTEE FUND



Channa de Silva
Director General
Securities & Exchange Commission of Sri Lanka
Trustee



Gamini Wickramasinghe
Chairman
Securities & Exchange Commission of Sri Lanka
Trustee

Colombo.
12th February 2007

Settlement Guarantee Fund

Income and Expenditure Statement

for the year ended 31st December 2006

INCOME	2006 Rs	2005 Rs
Interest on Investments - Treasury Bills	11,131,267	7,955,051
	<u>11,131,267</u>	<u>7,955,051</u>
Less:		
EXPENDITURE		
General Expenses	223	11,500
Custodian Fess	43,374	55,661
Audit Fees	17,933	50,000
Total Expenditure	<u>61,537</u>	<u>117,161</u>
Excess Income over Expenditure for the Year	<u>11,069,737</u>	<u>7,837,890</u>

The notes appearing on pages 68 to 71 form an integral part of the Financial Statements.

Settlement Guarantee Fund

Statement of Changes in net Assets

for the year ended 31st December 2006

	2006 Rs.	2005 Rs.
Accumulated Fund		
Balance at the beginning of the period	61,593,603	53,755,713
Net Surplus for the period	11,069,737	7,837,890
Balance at the end of the period	72,663,340	61,593,603

The notes appearing on pages 68 to 71 form an integral part of the Financial Statements.

Settlement Guarantee Fund

Cash Flow Statement

for the year ended 31st December 2006

	Notes	2006 Rs.	2005 Rs.
Cash Flow from Operating Activities			
Net Surplus for the year		11,069,737	7,837,890
Adjustment for			
Change of Working Capital			
(Increase)/Decrease of other receivable	2	(3,133,218)	(5,479,542)
Increase/(Decrease) of other payable	3	17,104	75,803
		(3,116,114)	(5,403,739)
Net Cash Flow from operating activities		7,953,623	2,434,151
Net Cash Flow from Financing Activities		-	-
Cash Flow from Investing Activities			
Investment in Treasury Bills		(7,933,900)	(2,448,257)
Net Cash Flow from Investing Activities		(7,933,900)	(2,448,257)
Net Increase(Decrease) in cash and cash equivalents		19,723	(14,106)
Cash & Cash Equivalents at beginning of the period		15,602	29,708
Cash & Cash Equivalents at the end of the period		35,325	15,602

The notes appearing on pages 68 to 71 form an integral part of the Financial Statements.

Settlement Guarantee Fund

Notes to the Financial Statements

1. ACCOUNTING POLICIES

1.1 BASIS OF PREPARATION

The Financial Statements of the Fund are presented in Sri Lankan Rupees rounded to the nearest Rupee.

The Financial Statements are prepared on the basis of historical cost convention. Where appropriate accounting policies are disclosed in succeeding notes.

1.2 STATEMENT OF COMPLIANCE

The financial statements of the Settlement Guarantee Fund are prepared in accordance with the Sri Lanka Accounting Standards and are in compliance with the said standards.

1.3 INVESTMENT

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

1.4 CONTINGENT LIABILITIES

There were no contingent liabilities as at 31st December 2006.

1.5 EVENTS OCCURRING AFTER THE BALANCE SHEET DATE

No material events occurred after the Balance Sheet date necessitating any adjustments or disclosure in the Financial Statements.

1.6 RETIREMENT BENEFIT

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

1.7 COMPARATIVE FIGURES

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

1.8 REVENUE RECOGNITION

Interest income is accounted on accrual basis

1.9 EXPENDITURE RECOGNITION

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

2.0 CASH FLOW STATEMENT

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

Settlement Guarantee Fund
Notes to the Financial Statements Contd...

2 RECEIVABLES	2006	2005
	Rs.	Rs.
Treasury Bill Interest Receivable	10,088,582	6,955,364
	10,088,582	6,955,364

3 PAYABLES	2006	2005
	Rs.	Rs.
Custodian Fees	57,745	40,641
Audit Fees	100,000	100,000
	157,745	140,641

4 RELATED PARTY TRANSACTIONS

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

As mentioned above by virtue of holding office the following were appointed as Trustees of the Fund during the year.

- Mr Gamini Wickramasinghe Chairman SEC appointed on 03rd February 2006.
- Mr Nihal Fonseka Chairman CSE appointed on 23rd May 2006.
- Mrs Sureka Sellahewa Director General CSE appointed on 1st July 2006.

The following Trustees resigned during the year.

- Mr Eraj Wijesinghe former Chairman CSE assumed duties as a Trustee on 15th March 2003 and ceased to be a Trustee upon expiration of his term of office with effect from 23rd May 2006.
- Mr Hiran Mendis former Director General CSE assumed duties as a Trustee from the inception of the Fund and resigned with effect from 16th July 2006.

Settlement Guarantee Fund

Notes to the Financial Statements Contd...

The following table depicts the relationships held by the present Trustees of the Fund as at 31st December 2006.

Name of the Trustee	Name of related Institution	Relationship
Mr G Wickramasinghe	Informatics (Pvt) Ltd	Director
	Informatics Institute of Technology Ltd	Director
	Informatics Information Systems (Pvt) Ltd	Director
	Informatics Agrotech (Pvt) Ltd	Director
	Visual Computing Systems (Pvt) Ltd	Director
	Informatics International Ltd	Director
	Informatics Hospitality Systems Ltd	Director
	Informatics International Lanka (Pvt) Ltd	Director
	Informatics Holdings Ltd	Director
	Charles Exports (Pvt) Ltd	Director
	Industrial and Financial Systems Solutions Ltd	Director
	Systems Integrators (Private) Ltd	Director
	Informatics Trading (Private) Ltd	Director
	Industrial and Financial Systems Sri Lanka Ltd	Director
Insurance Board of Sri Lanka	Chairman	
Securities and Exchange Commission of Sri Lanka	Chairman	
Mr Nihal Fonseka	DFCC Stockbrokers (Pvt) Ltd	Chairman
	Lanka Industrial Estates Ltd	Chairman
	Lanka Ventures Ltd	Chairman
	Synapsys Ltd	Chairman
	DFCC Bank	Director
	DFCC Consulting (Pvt) Ltd	Director
	National Asset Management Ltd	Director
	Colombo Stock Exchange	Chairman / Director
	Commercial Bank of Ceylon Ltd	Director
	Commercial Bank Primary Dealer Ltd	Director
	Credit Information Bureau of Sri Lanka	Director
	ONEzero Co Limited	Director
	National Institute of Business Management	Member (Ex-officio)
Postgraduate Institute of Management	Member	
Mr Sumith Abeysinghe	Bank of Ceylon	Director (Treasury Nominee)
	Securities and Exchange Commission of Sri Lanka	Member (Treasury Nominee)
	Insurance Board of Sri Lanka	Member (Treasury Nominee)
	Southern Development Authority	Director (Treasury Nominee)
	De-La Rue Lanka	Director (Treasury Nominee)
Mr Channa de Silva	Insurance Board of Sri Lanka	Member
	Public Enterprises Reforms Commission of Sri Lanka	Member
	Sri Lanka Accounting & Auditing Standards Monitoring Board	Member
	Construction Guarantee Fund	Trustee
	Public Sector Infrastructure Development Co. Ltd.	Director
	Securities and Exchange Commission of Sri Lanka	Director General
Mrs Sureka Sellahewa	Colombo Stock Exchange	Director General

Settlement Guarantee Fund

Notes to the Financial Statements Contd...

The following table depicts relationships held by the Trustees of the Fund who resigned during the year under review.

Name of the Trustee	Name of the related Institution	Relationship
Mr Eraj Wijesinghe	Bartleet & Company Ltd	Chairman
	Bartleet Agencies Ltd	Chairman
	Bartleet Electronics Ltd	Chairman
	Bartleet Financial Services Ltd	Chairman
	Bartleet Mallory Stockbrokers (Pvt) Ltd	Chairman
	Bartleet Asset Management (Pvt) Ltd	Chairman
	Bartleet Mecklai & Roy Ltd	Chairman
	Bartleet Microdevices Lanka (Pvt) Ltd	Chairman
	Bartleet Produce Marketing (Pvt) Ltd	Chairman
	Bartleet Technologies (Pvt) Ltd	Chairman
	BC Agro-Tronics (Pvt) Ltd	Chairman
	Associated Castloy Engineers (Pvt) Ltd	Chairman
	BC Computers Ltd	Chairman
	Enterprise Technology (Pvt) Ltd	Chairman
	BC Software Systems (Pvt) Ltd	Chairman
	Ceylon Quartz Industries (Pvt) Ltd	Chairman
	Colombo Stock Exchange	Chairman
	Sky Travels Ltd	Chairman
	LIC Lanka (Pvt) Ltd	Director
	Bartleet TransCapital (Pvt) Ltd	Director
Ceylon Asset Management Co Ltd	Director	
Unik Agencies (Pvt) Ltd	Director	
Yoropa Investments & Trading (Pvt) Ltd	Director	
Mr Hiran Mendis	Colombo Stock Exchange	Director General

The Settlement Guarantee Fund other than the transactions in the ordinary course of business at market rates no transactions were recorded with the said institutions during the year.

Settlement Guarantee Fund
Auditors Report



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கணக்காய்வாளர் தலைமை அறிப்பறி திணைக்களம்
AUDITOR-GENERAL'S DEPARTMENT



මගේ අංකය. }
எனது இல. } LP/F/SEC/2007/01
My No. }

ඔබේ අංකය. }
உமது இல. }
Your No. }

දිනය. }
திகதி. } 09th July 2007
Date. }

The Chairman,
Settlement Guarantee Fund
Securities and Exchange Commission of Sri Lanka

Report of the Auditor General on the Financial Statements of the Settlement Guarantee Fund for the Year ended 31st December 2006

The Audit of the Financial Statement of the Settlement Guarantee Fund for the year ended 31st December 2006 was carried out under my direction in pursuance of provisions in Article 154(3) of the Constitution of the Democratic Socialist Republic of Sri Lanka read in conjunction with paragraph 11(d) of the Deed of Trust No. 1376 dated 21/22 May 1998 in respect of Settlement Guarantee Fund created by the Securities and Exchange Commission of Sri Lanka.

1:2 Scope of Audit

Audit opinion, comments and findings in this report are based on a review of the financial statements presented to audit and substantive test of samples of transactions. The scope and the extent of such review and tests were such as to enable as wide an audit coverage as possible within the limitation of staff, other resources and time available to me. The audit was carried out in accordance with Sri Lanka Auditing Standards, methods and practices to obtain reasonable assurance as to whether the financial statements are free of material misstatements. The audit included examination of evidence supporting the amounts and disclosures in financial statements and assessment of accounting principles and significant estimates and judgements made in the preparation of financial statements, evaluation of their overall presentation and determining whether accounting policies adopted were appropriate, consistently applied and adequately disclosed.

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கொடை 07, ශ්‍රී ලංකාව.

சுதந்திர சதுக்கம்,
கொழும்பு 07, சிலங்கை

INDEPENDENCE SQUARE,
COLOMBO 07, SRI LANKA.

දුරකථනය }
தொலைபேசி } 2691151
Telephone }

ලැයිස් අංකය }
பக்ஸ் இல. } 2697451
Fax No. }

ඉලෙක්ට්‍රොනික් තැපෑල }
✉-மேயில் } oaggov@sltnet.lk
E-mail }

2. Accounts

2:1 Opinion

So far appears from my examination and to the best of my information and according to the explanations given to me, I am of opinion that the Settlement Guarantee Fund had maintained proper books of account for the year ended 31 December 2006 and the financial statements which are in agreement with the said books have been prepared and presented in accordance with Sri Lanka Accounting Standards and the stated accounting policies and notes (Nos. 1 to 4) to the financial statements give a true and fair view of the financial position of the Fund as at 31 December 2006, and the financial results of its operations and cash flow for the year then ended.

2:2 Financial Results

According to the financial statements presented, the activities of the fund for the year under review had resulted in a surplus of Rs. 11,069,737 as compared with the corresponding surplus of Rs 7,837,890 for the preceding year.

3 Operating Review

3:1 Functions of the Funds

Disputes between Clearing Members of the Central Depository System had not been reported from the inception of the Fund through the paragraph 5(a) of the Deed of Trust No. 1376 dated 21/22 May 1998 provides for settlement of such disputes.

3:2 Investments

Action had not been taken to transfer the investments held in Treasury Bills as at 31 December 2006 amounting to Rs. 112,697,178 to the "State Institutions Temporary Surplus Trust Fund" in terms of the Public Enterprises Circulars No. PED 33 of 19 December 2005 and No. 30 of 13 July 2005.



(P A PEMATILAKA)
AUDITOR GENERAL

Responses of the Commission to the matters raised by the Auditor General

Auditor General's Observation	SEC responses
<p>3. Operating Review</p> <p>3.1 Functions of the Fund</p> <p>Disputes between Clearing Members of the Central Depository System had not been reported from the inception of the Fund through the paragraph 5(a) of the Deed of Trust No 1376 dated 21/22 May 1998 provides for settlement of such disputes.</p> <p>3.2 Investments</p> <p>Action had not been taken to transfer the investments held in treasury Bills as at 31st December 2006 amounting to Rs. 112,697,178 to the "State Institutions Temporary Surplus Fund" in terms of the Public Enterprises Circular No PED 19th December 2005 and No 30 of 13th July 2005.</p>	<p>Your comment is correct. Since the inception of the Settlement Guarantee Fund (SGF) no disputes were reported to the Commission between the Clearing Members of the Central Depository System.</p> <p>Your comment noted. This issue will be taken up at the next meeting of the Trustees.</p>

Corporate Information

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Echelon Square, Colombo 01, Sri Lanka.

Tel : 2331013-6, 2439144-8

Fax : 2439149

E-mail : mail@sec.gov.lk

Web : www.sec.gov.lk

Legal Form : Securities and Exchange Commission of Sri Lanka
was incorporate by Act No 36 of 1987 as amended
by Act No 26 of 1991 and Act No 18 of 2003

Accounting Year end : 31 December

Auditors : The Auditor General

Bankers : The Bank of Ceylon
Standard Chartered Bank
Sampath Bank
Hongkong & Shanghai Banking Corporation Limited

