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Enclosed: Form of Proxy

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This Annual Report is published within three months of the Balance Sheet date and the HTML version in addition to the PDF version is also published on-line on the same date as the date of issue of this Report. ([www.combank.net](http://www.combank.net))

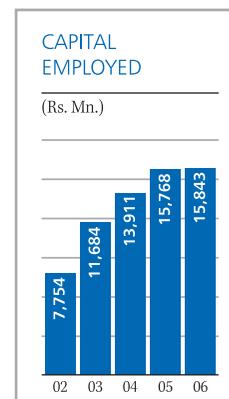
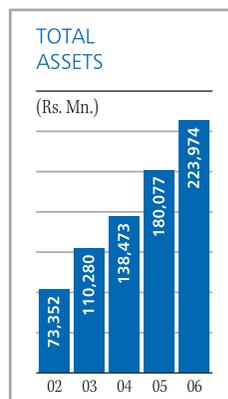
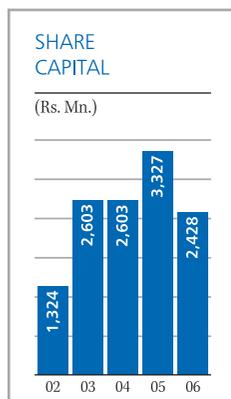
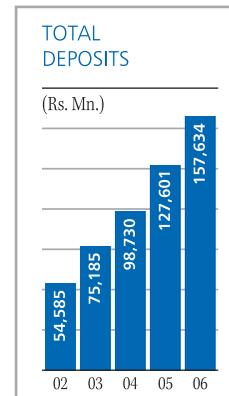
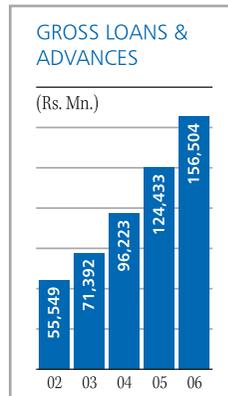
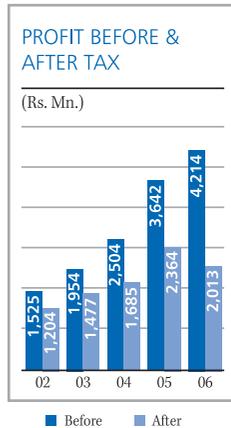
The last decade was a high growth decade for the Bank.  
Today, Commercial Bank is the largest and the most admired private Bank in Sri Lanka.  
The next decade will see a quantum leap in growth.

Our New **MISSION**

**Redefining  
convenience  
in financial  
services**

will guide the underpinnings of this growth.

Our New **VISION** is  
To be the **PREFERRED** financial services  
organization in Sri Lanka, having an  
international presence  
by the year 2011



## Financial Goals & Achievements

Financial Indicator (%)	Goal	Achievements				
		2006	2005	2004	2003	2002
Return on Average Assets	Over 2	<b>1.00</b>	1.48	1.35	1.61	1.82
Return on Average Shareholders' Funds	Over 20	<b>12.73</b>	15.93	13.16	15.20	16.61
Growth in Income	Over 20	<b>51.99</b>	31.00	22.17	20.26	1.96
Growth in Profit after Taxation	Over 20	<b>(14.87)</b>	40.33	14.03	22.71	19.21
Growth in Total Assets	Over 20	<b>24.38</b>	30.04	25.57	50.34	24.02
Dividend Rate	Over 40	<b>50.00</b>	45.00	60.00	50.00	50.00
<b>Capital Adequacy Ratios (Group)</b>						
Tier I	Over 8	<b>7.62</b>	9.68	10.78	13.43	14.94
Tier I & II (Total Capital)	Over 13	<b>11.58</b>	12.08	13.16	15.46	15.07

	<b>Bank</b>			<b>Group</b>		
	<b>2006</b>	2005	Change	<b>2006</b>	2005	Change
	<b>Rs. Mn.</b>	Rs. Mn.	%	<b>Rs. Mn.</b>	Rs. Mn.	%
<b>Results for the year</b>						
Income	<b>24,469.470</b>	16,099.645	51.99	<b>24,451.866</b>	16,225.377	50.70
Profit before Taxation	<b>4,213.545</b>	3,641.960	15.69	<b>4,321.153</b>	3,668.048	17.81
Provision for Taxation	<b>2,200.917</b>	1,277.720	72.25	<b>2,248.751</b>	1,309.969	71.66
Profit after Taxation	<b>2,012.628</b>	2,364.240	(14.87)	<b>2,072.402</b>	2,358.079	(12.11)
Revenue to the Governments	<b>3,169.017</b>	1,917.475	65.27	<b>3,216.851</b>	1,951.393	64.85
Gross Dividends	<b>911.413</b>	869.717	4.79	<b>911.413</b>	869.717	4.79
<b>At the year end</b>						
Shareholders' Funds (Capital and Reserves)	<b>15,842.841</b>	15,768.383	0.47	<b>16,016.460</b>	15,953.573	0.39
Deposits from Customers	<b>157,634.070</b>	127,601.280	23.54	<b>157,531.828</b>	127,490.713	23.56
Gross Loans & Advances to Customers	<b>156,503.730</b>	124,433.419	25.77	<b>156,401.538</b>	124,350.117	25.78
Total Assets	<b>223,974.253</b>	180,077.463	24.38	<b>224,060.639</b>	180,135.051	24.38
<b>Information per Ordinary Share</b>						
Earnings (Basic) (Rs.)	<b>12.71</b>	14.94	(14.93)	<b>13.12</b>	14.89	(11.89)
Dividends (Rs.)	<b>5.00</b>	4.50	11.11	<b>5.00</b>	4.50	11.11
Net Assets Value per Ordinary Share (Rs.)	<b>103.93</b>	97.06	7.08	<b>105.14</b>	98.36	6.89
Market Value at the year end - Voting (Rs.)	<b>190.00</b>	135.50	40.22	<b>190.00</b>	135.50	40.22
Market Value at the year end - Non-Voting (Rs.)	<b>89.00</b>	57.50	54.78	<b>89.00</b>	57.50	54.78
<b>Ratios</b>						
Return on Average Shareholders' Funds (%)	<b>12.73</b>	15.93	(20.09)	<b>12.96</b>	15.69	(17.40)
Return on Average Assets (%)	<b>1.00</b>	1.48	(32.43)	<b>1.03</b>	1.47	(29.93)
Price Earnings (times) - Ordinary Voting Shares	<b>14.95</b>	9.02	65.74	<b>14.47</b>	7.44	94.49
Price Earnings (times) - Ordinary Non-Voting Shares	<b>7.00</b>	3.83	82.77	<b>6.78</b>	4.19	61.81
Year on year Growth in Earnings (%)	<b>(14.87)</b>	40.33	(136.87)	<b>(12.11)</b>	36.53	(133.15)
Year on year Growth in Dividends on Ordinary Shares (%)	<b>11.11</b>	(25.00)	144.44	<b>11.11</b>	(25.00)	144.44
Dividend Yield (%) - Ordinary Voting Shares	<b>2.63</b>	3.32	(20.78)	<b>2.63</b>	3.32	(20.78)
Dividend Yield (%) - Ordinary Non-Voting Shares	<b>5.62</b>	7.83	(28.22)	<b>5.62</b>	7.83	(28.22)
Dividend Cover on Ordinary Shares (Times)	<b>2.54</b>	3.34	(23.95)	<b>2.63</b>	3.33	(21.02)
Dividend Cover on Preference Shares (Times)	<b>10.19</b>	10.26	(0.68)	<b>10.50</b>	10.24	2.54
Total Dividend Cover (times)	<b>2.21</b>	2.72	(18.75)	<b>2.27</b>	2.71	(16.24)
<b>Statutory Ratios</b>						
Liquid Assets (%)	<b>22.64</b>	24.51	(7.63)	<b>22.64</b>	24.51	(7.63)
<b>Capital Adequacy -</b>						
Tier I (%) - Minimum Required 5%	<b>7.61</b>	9.64	(21.06)	<b>7.62</b>	9.68	(21.28)
Tier I & II (%) - Minimum Required 10%	<b>11.56</b>	12.03	3.91	<b>11.58</b>	12.08	(4.14)

# DEAR SHAREOWNER, HAVING ESTABLISHED ITS POSITION AS A TRENDSETTER AND THE PREMIER FINANCIAL INSTITUTION, THE BANK IS POISED TO MAKE A QUANTUM LEAP OVER THE NEXT FEW YEARS



The Bank soon hopes to be a global player delivering its high quality and state-of-the-art products to diverse customers in different parts of the world.

The Bank will focus on making itself more accessible to its customers in terms of delivery channels, products, technology and overall convenience. Our goal is to provide a broad array of options and make banking and financial services truly customer friendly.

The Bank concluded yet another remarkable year in 2006. Our performance is even more creditable given the tough external environment. It is a testimony to the Bank's resilience that it is able to perform and perform extremely well, in good times and in bad.

The Bank retained the AA+ (lka) national rating, by Fitch Ratings Lanka Ltd. (FRL), for its implied long-term unsecured senior debt and maintained its position as the indigenous private bank with the highest rating from FRL.

Despite an uncertain security scenario, the Bank, its subsidiaries and associate companies marked yet another exceptionally successful year, recording a pre-tax profit (before the Financial Value Added Tax on profit) of Rs. 5.292 billion

for 2006. This is a growth of Rs. 999.458 million or 23.28% over the previous year.

The Financial Value Added Tax calculated on the basis of 20% of the staff emoluments and the pre-tax profit (after charging it) amounted to Rs. 970.958 million. After providing for this Financial Value Added Tax, the profit before corporate tax amounted to Rs. 4.321 billion, a growth of Rs. 653.105 million or 17.81%.

This profit includes a gain of Rs. 749.800 million realised on the disposal of DFCC shares and an initial provision of Rs. 1.654 billion to the restructured pension scheme, two exceptional items during the year. However, after discounting for the above two items, the Group recorded a normalised pre-tax profit of Rs. 5,074.624 million, an impressive growth of Rs. 1,406.576 million or 38.34% over the previous year.

Post-tax profit of the Bank for the year amounted to Rs. 2.013 billion compared to Rs. 2.364 billion recorded for 2005. The main reason for the decrease in post-tax profit was the increase in the provision for corporate tax from Rs. 1.278 billion in 2005 to Rs. 2.201 billion in 2006 mainly due to the increase in corporate tax rate from 30% to 35% in 2006 and a sum of Rs. 1,669.7 million out of the provision for the restructured pension scheme being disallowed for tax purposes.

The normalised post-tax profit of the Bank amounted to Rs. 2,766.099 million, representing a growth of Rs. 401.860 million or 17.00% over the previous year.

A 5.37% depreciation of the Rupee during 2006 helped to boost the exchange profit to Rs. 1,439.008 million for 2006 compared to an exchange profit of Rs. 586.915 million in the previous year.

Commission and other income recorded a growth of Rs. 251.581 million to reach Rs. 2,011.285 million, up by 14.30% compared to the previous year. Total operating expenses including the loan losses and provisions increased from previous year's Rs. 5,231.625 million to Rs. 8,301.315 million in 2006 recording an increase of 58.68%.

Total deposits rose from Rs. 127.601 billion at the end of 2005 to Rs. 157.634 billion at the end of 2006. This represents a growth of Rs. 30.033 billion or 23.54%. Net loans, advances and leases rose from Rs. 118.763 billion to Rs. 150.532 billion, a growth of Rs. 31.769 billion or 26.75%.

The Group's total assets grew from Rs. 180.135 billion to Rs. 224.061 billion at end 2006 representing a growth of Rs. 43.926 billion or 24.38%.

The Bank ended 2006 as the largest indigenous private sector bank in the country. The Bank's market capitalisation at the year end was the highest among all financial institutions in Sri Lanka.

An interim dividend of 15% was paid by the Bank in November 2006. A final dividend of 35% has been recommended by the Directors for your approval, thus bringing the total dividends for 2006 to 50%, as against total dividends of 45% paid for 2005.

As you may be already aware, subject to the receipt of the necessary regulatory and shareholder approvals, the Boards of Directors of your Bank and the NDB bank announced in January 2007 their decisions to explore the feasibility of merging the two banks. Given the respective strengths, the two banks believe that a merger will help in realising potential synergies and in exploiting opportunities in the international markets.

Further, subject to the receipt of the necessary approvals from the Colombo Stock Exchange and the shareholders, your Board of Directors, announced a rights issue of ordinary shares on the basis of three new ordinary shares for every ten existing ordinary shares at Rs. 138/- and Rs. 65/- for voting and non-voting shares respectively, to be followed by a scrip issue of ordinary shares on the basis of one share for every three shares held on the enhanced share capital consequent to the proposed rights issue. The purpose of the proposed rights issue is to strengthen the capital funds position and to support the future expansion projects of the Bank.

### **Supplementing Deposit Mobilisation**

In 2005, the Bank successfully mobilised Rs. 1.309 billion through a debenture issue.

A further Rs. 2.127 billion was raised in 2006, through the issue of two series of Unsecured Subordinated Redeemable Debentures. The funds raised will supplement deposit mobilisation and help the expansion of the medium to

long-term loan book of the Bank while further strengthening the funding mix of the Bank.

Towards the end of 2006, the Bank mobilised US \$ 10 million through an issue of a 5-year bond, the first time the Bank has raised funds for such a long period in US \$ bonds. This is the first time that an indigenous bank in Sri Lanka had raised capital through a bond denominated in foreign currency.

We have been able to supplement the deposit mobilisation efforts as detailed above given that we have been able to sustain our AA+ (lka) credit rating despite the volatile political conditions.

The Statutory Liquid Assets Ratio (SLAR) and working liquidity of the Bank have also improved as a result of the funds so mobilised. Since the last issue of debentures is listed in the Colombo Stock Exchange, it has provided members of the public with an opportunity to invest in a tradable security that has been assigned AA (lka) rating by FRL.

All these debt issues qualify as Tier II capital, strengthening further the Capital Adequacy Ratio of the Bank.

### **Corporate Responsibility under independent scrutiny**

This year the Bank took the bold step of opening up its Corporate Responsibility for scrutiny by the global agency Det Norske Veritas popularly known as DNV. This makes Commercial Bank the first company in the Asian region to voluntarily throw

itself up for such independent expert evaluation. We are proud of the B+ rating that the Bank has earned for its Corporate Responsibility. In keeping with emerging global trends of good reporting, the Board decided to publish DNV's Corporate Responsibility Rating Report which appears on pages 37 to 45 of this Annual Report.

### **Best Bank for Eight Years**

The Bank continued to win many awards and accolades in 2006. The prestigious US based 'Global Finance Magazine' chose Commercial Bank as 'The Best Bank in Sri Lanka' for the eighth consecutive year. The criteria for choosing the winner included growth in assets, profitability, capital strength, strategic relationships, customer service, competitive pricing and innovative products.

### **Overall Winner of Business Excellence**

The Bank qualified for a number of awards at the recently held National Business Excellence Awards 2006, organised by the National Chamber of Commerce. The Bank won the Overall Award for Business Excellence, the Extra Large Category Award, the Block Buster Performance Award, the Overall Award in the Banking Sector and the Award for Business and Financial Sustainability.

The Bank was also conferred 'Silver' and 'Merit' Awards in the Financial Category at the National Best Quality Software Awards (NBQSA) 2006 competition conducted by the Sri Lankan section of the British

Computer Society. 'Com e-Load' won the Silver Award in the Financial Category while 'ComBank Online' won the Merit Award in the same Category.

### **Best Annual Report for Five Years Running**

The Bank's Annual Report for 2005 won the Overall Award and the Award in the Banking Institutions Sector for the fifth consecutive year at the Annual Report Awards Competition organised by The Institute of Chartered Accountants of Sri Lanka (ICASL).

At the recent South Asian Federation of Accountants (SAFA) Awards too the Bank's Annual Report was placed first in the Banking Sector for the fifth consecutive year. In addition, it also won the award for the Best Corporate Governance Disclosures and was placed the second runner-up in the overall category. These awards are ample testimony to our commitment to transparency and disclosure.

### **Investing in the Next Generation**

Under a new CSR project launched last year, the Bank presented 100 scholarships to undergraduates from different parts of the country. Each scholarship provides Rs. 2,500/- a month for 10 months of a calendar year during the period of study in the university. This is the first time the Bank has got involved in a project on higher education. The undergraduates were chosen in collaboration with the University Grants Commission and according to the criteria used by the Mahapola Scholarship Scheme.

Commercial Bank also assisted ten families living in the Matara District who had lost their homes due to the tsunami which occurred in 2004. They were provided with new homes by the Bank at a cost exceeding Rs. 5 million.

The Bank donated Rs. 2 million towards the South Asian Games held in Colombo and also provided a public address system to the Government Hospital at Karapitiya at a cost of over Rs. 600,000/-.

### Building a Sustainable Economy

The Government must soon offer a political solution with a view to resolving the ethnic conflict. Such a political solution will hopefully set in motion a process that will create the conditions for a sustainable and dynamic economy.

The GDP is estimated to have recorded an impressive growth of 7% in real terms in 2006. The budget deficit was contained at 8.7% of GDP in 2006 according to revised figures. This is a reduction from the figure of 9.1% budgeted earlier for 2006.

Unemployment had declined to 6.4% by the end of the third quarter of 2006, one of the lowest rates recorded after Sri Lanka gained independence.

Favourable weather, while boosting agricultural production, helped to increase hydro-electricity generation and reduced the dependence on thermal power generation, making a significant contribution to overall economic growth.

While acknowledging the resilience of the Sri Lankan economy and its favourable medium-term growth prospects, it is imperative that the Government pays more attention to fiscal discipline and concentrate on enhancing its revenue while combating corruption and wastage. Failure to do so will result in ballooning budget deficits, which in turn would exert inflationary pressures leading to high interest rates.

Policy consistency is an area in which Sri Lanka has had a poor record. In this regard, I welcome the establishment of the Economic Advisory Council and the Expert Panel set up by the Central Bank.

The Government's emphasis on infrastructure development, including power and roads, augurs well. According to the budget for 2007, the proposed increase in public investments from Rs. 162.242 billion in 2006 to Rs. 240.422 billion in 2007 will boost long-term growth potential.

### Transforming into a Global Player

We have set our sights on the region and beyond and will soon begin to establish our presence in different parts of the world. We hope we can bring the innovation and dynamism that have transformed our Sri Lankan operation, to our operations in other parts of the world.

### A Team Effort

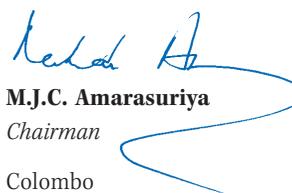
Our staff, under the guidance of the Managing Director, played a pivotal role in this magnificent performance. I would like to acknowledge their role and applaud their efforts.

My thanks also go to my colleagues on the Board for the inspiration and the guidance they have provided to the Institution.

I take this opportunity to thank Mr. J.S. Mather, our former Deputy Chairman, who resigned last year, after 17 years of service. I also wish to thank Mr. Sanjiva Senanayake for his services to the Bank and warmly welcome Mr. G. Galludec who replaced him on the Board. I extend a warm welcome to Deshamanya Ken Balendra who joined the Board during the year.

It is with a profound sense of sadness that I record the deaths of Mr. M.R.V. de Almeida, a former Managing Director of Commercial Bank and Dr. M.J.P. de Silva, a former Director of the Bank. On behalf of the Bank, I offer my sincere condolences to the members of their families.

We look forward to another challenging year and a year of transformation as the Bank seeks new borders and a new niche in the regional and global financial world.

  
**M.J.C. Amarasuriya**  
 Chairman

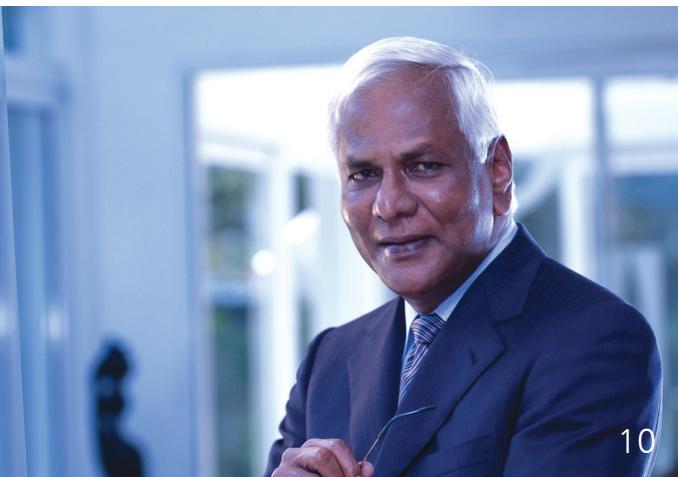
Colombo  
 February 15, 2007

## Board of Directors



01. M.J.C. Amarasuriya (*Chairman*)
02. B.R.L. Fernando (*Deputy Chairman*)
03. A.L. Gooneratne (*Managing Director*)
04. Dr. H.S. Wanasinghe
05. A.N. Fonseka
06. Lalin J.A. Fernando
07. Iyad M. Malas
08. Dinesh Weerakkody
09. G. Galludec (*Alternate to Iyad M. Malas*)
10. Deshamanya Ken Balendra
11. Mrs. R.R. Dunuwille (*Company Secretary*)





## Board of Directors

### **M.J.C. Amarasuriya** - *Chairman*

First appointed to the Board on May 15, 1986 and appointed Chairman on January 1, 1995.

No. of Shares held: 309,864 (Voting) and 104,932 (Non-Voting).

Chairman of  
Pelwatte Sugar Industries Ltd.  
Serendib Flour Mills (Pvt.) Ltd.  
Equity Investments Lanka Ltd.  
Commercial Fund Management (Pvt.) Ltd.

Director of  
Commercial Leasing Co. Ltd.

Past Chairman of  
Joint Business Forum of Chambers of Commerce and Industry, Employers' Organisations and Trade Associations of Sri Lanka (JBIZ).

The Employers' Federation of Ceylon.

International Chamber of Commerce, Sri Lanka.

Regional Industry Service Committee of the North-Western Province.

Former Deputy Chairman of  
Hayleys Ltd.

### **B.R.I. Fernando** - *Deputy Chairman*

First appointed to the Board on January 1, 1995 and appointed Deputy Chairman on April 6, 2006.

No. of Shares held: 4,778 (Non-Voting)

Fellow of The Institute of Chartered Accountants of Sri Lanka

Chairman of  
Chemical Industries (Colombo) Ltd.  
CIC Fertilizers (Pvt) Ltd.  
CIC Seeds (Pvt) Ltd.  
CIC Feeds (Pvt) Ltd.  
CIC Vetcare (Pvt) Ltd.  
CIC Agri-biotech (Pvt) Ltd.  
CIC Poultry Farms Ltd.  
CIC Bio Security Breeder Farms Ltd.  
CISCO Speciality Packaging (Pvt) Ltd.

Director of  
Rainwear (Pvt) Ltd.

Trustee of The Employers' Federation of Ceylon

Possesses extensive experience in Finance and Commerce.

### **A.L. Gooneratne** - *Managing Director*

First appointed to the Board as the Managing Director on January 6, 1997.

Joined the Bank in March 1983 and held several senior positions prior to his appointment as the General Manager/Chief Executive in March 1996.

No. of Shares held: 390,158 (Voting) and 17,324 (Non-Voting).

Fellow of The Institute of Chartered Accountants, England & Wales.

Director of  
The Financial Ombudsman, Sri Lanka (Guarantee) Ltd.

Council Member of  
The Employers' Federation of Ceylon.

Former Chairman of  
The Sri Lanka Banks' Association (Guarantee) Ltd.

Represents the Bank's interests on the Boards of all of its Associate and Subsidiary Companies.

### **Dr. H.S. Wanasinghe**

First appointed to the Board on January 5, 1990.

No. of Shares held: Nil.

Senior Visiting Fellow of the Institute of Policy Studies.

Member of  
Council of Fellows of the Marga Institute.

Member of  
Board of Directors of the Centre for Policy Alternatives.

Director of  
Commercial Development Co. Ltd.

Served the United Nations Economic and Social Commission for Asia and the Pacific for 15 years and on return to Sri Lanka in 1986 served as the Chairman of the Presidential Committee on Administrative Reforms, the Presidential Taxation Commission and the Public Investment Management Board. Before joining the United Nations, served as a Member of the Ceylon Civil Service for 24 years.

### **A.N. Fonseka**

First appointed to the Board on January 31, 2000.

No. of Shares held: 622 (Non-Voting).

Director of  
DFCC Bank (General Manager/Chief Executive)

Chairman of  
Colombo Stock Exchange.

Vice-Chairman of  
Association of Development Financing Institutions in Asia and the Pacific (ADFIAP).

Member - Governing Board of  
The National Institute of Business Management.  
Post Graduate Institute of Management,  
University of Sri Jayawardenapura

Member of  
Financial Sector, Capital Markets and Taxation  
Clusters of the National Council for Economic  
Development (NCED)

Committee Member of  
The Ceylon Chamber of Commerce.

### **Lalin J.A. Fernando**

First appointed to the Board on April 25, 2003.

No. of Shares held: Nil.

Founder & Managing Director of  
Standard Trading Company (Pvt) Ltd.

Director of  
L.F. Holdings (Pvt) Ltd.  
L.F. Teas (Pvt) Ltd.  
STC Logistics (Pvt) Ltd.  
STC Trading House (Pvt) Ltd.  
Motor Marvels (Pvt) Ltd.  
Frontier Automotive (Pvt) Ltd.  
Koboshu Corporation (Pvt) Ltd.  
Horana Plantations Ltd.  
Unidil Packaging (Pvt) Ltd.  
Ceytea Plantation Management Ltd.  
Research International (Pvt) Ltd.  
Marlinkspike Property Developers (Pvt) Ltd.

Counts over 35 years experience in the Tea Trade and Private Sector Management.

**Iyad M. Malas**

First appointed to the Board on November 23, 2004.

No. of Shares held: Nil.

Holds an MBA from George Washington University and is a Chartered Financial Analyst.

Has been with the World Bank Group since 1987 and was previously a Manager in the IFC's Central Asia, Middle East and North Africa Department.

As Head of the investment bank, Fleming CIIC in Cairo, was responsible for the creation of the largest investment bank in the MENA region.

Instrumental in developing the Emerging Markets Data Base into a fully-fledged commercial product.

Extensive experience working in Latin America, Asia, South Europe and the Middle East.

Possesses extensive experience in the private sector and IFC including strong industry knowledge in General Manufacturing, Information Technology and Financial Markets.

**Dinesh Weerakkody**

First appointed to the Board on July 29, 2005.

No. of Shares held: Nil.

Graduate in Business Administration.

Holder of a Master's Degree in Business Administration (MBA) from the University of Leicester, England.

Associate of the Chartered Institute of Management Accountants, UK.

Managing Director of Cornucopia Lanka Ltd.

Director of DFCC Bank Smithkline Beecham Ltd.

Former Chairman/CEO of Employees' Trust Fund Board, Sri Lanka.

Advisor to the Prime Minister of Sri Lanka (January 2003 - April 2004).

Human Resource Director of Smithkline - Sri Lanka (January 1998 - November 2005).

Council Member of Chartered Institute of Management Accountants (CIMA) Sri Lanka Division. Sri Lanka Tennis Association

Has received extensive training in Human Resource Management in Singapore, London, Japan, India and in the USA.

**G. Galludec - Alternate Director to Iyad M. Malas**

First Appointed to the Board on July 6, 2006.

No. of Shares held: Nil.

Graduated from EM Lyon (France).

IFC Country Manager for Sri Lanka and Maldives and Program Manager - South Asia Enterprise Development Facility.

Previously worked in the European Investment Bank in Luxembourg.

First Secretary General of PlaNet Finance and has worked extensively in Micro finance and SME finance worldwide.

Over 20 years of experience in the banking sector with extensive work in Africa, Central Europe and Asia in managerial positions.

**Deshamanya Ken Balendra**

First appointed to the Board on October 02, 2006.

No. of Shares held: Nil.

Conferred the National Honour of Deshamanya by Her Excellency the President of Sri Lanka, in 1998, in recognition of distinguished services of a highly meritorious nature.

Voted as the most effective business leader in Sri Lanka since independence in an opinion poll conducted by the 'Lanka Monthly Digest' in October 2003 and selected as the 'Sri Lankan of the Year' by the same publication in 1998.

Co-chaired the Joint-Study Group which prepared the Indo-Sri Lanka Comprehensive Economic Partnership Agreement that was presented to the Prime Ministers of the two countries in 2003.

Appointed by Her Excellency the President of Sri Lanka to the Task Force for Rebuilding the Nation immediately after the tsunami disaster and has been focusing on the Roads and Bridges Sector.

Honorary Member of The Association of Hotel School Graduates. Tea Traders' Association.

Trustee of The Royal College Union. The George Keyt Foundation.

Chairman of Brandix Lanka (Pvt) Ltd. Ceylon Tobacco Co. Ltd.

South Asia Regional Fund, sponsored by the Commonwealth Development Corporation for investment in South Asia.

Investment Committee of Aureos South Asia Fund, a joint venture between the Commonwealth Development Corporation of UK and NORFUND of Norway.

The Board of Trustees of the National Council for Mental Health.

Investment Committee of Aureos Lanka Advisers Ltd.

Director of Caltex Lubricants Lanka Ltd. Honorary Consul-General for Poland.

Former Chairman of John Keells Holdings Ltd. Bank of Ceylon. Securities and Exchange Commission. Insurance Board of Sri Lanka. Ceylon Chamber of Commerce.

Immediate Past President of Sri Lanka Institute of Directors. Sri Lanka-India Society.

**Mrs. R.R. Dunuwille - (Company Secretary)**

Attorney-at-Law

Chartered Secretary (UK)

## Operating Highlights

BANK'S DEPOSITS GREW BY 23.54%  
TO REACH RS. 157.634 BILLION

BANK'S LOANS & ADVANCES GREW  
BY 25.77%  
TO REACH RS. 156.504 BILLION

THE GROWTH RATES OF BOTH  
DEPOSITS AND ADVANCES OF THE BANK ARE  
BELIEVED TO BE HIGHER THAN THE  
INDUSTRY AVERAGES

BANK'S TOTAL ASSETS GREW  
BY 24.38%  
TO REACH RS. 223.974 BILLION

BANK'S ROA DROPPED  
TO 1.00%  
2005 - 1.48%

BANK'S NON-PERFORMING ASSETS  
RATIO (NPA)  
2.74%  
2005 - 3.22%

BANK'S PROVISION COVER  
60.41%  
2005 - 53.85%

GROUP'S PRE-FINANCIAL VAT AND  
PRE-TAX PROFIT  
RS. 5.292 BILLION  
2005 - RS. 4.293 BILLION

GROUP'S PRE-TAX PROFIT  
RS. 4.321 BILLION  
2005 - RS. 3.668 BILLION

GROUP'S POST-TAX PROFIT  
RS. 2.072 BILLION  
2005 - RS. 2.358 BILLION

GROUP'S CAPITAL ADEQUACY  
RATIOS TIER I & TIER I & II  
7.62% & 11.58%  
2005 - 9.68% & 12.08%

# A REMARKABLE PERFORMANCE IN A TURBULENT YEAR

Commercial Bank had a remarkable year in a tough operating environment. The Bank's performance in 2006, in varying and turbulent conditions, exhibits its indomitable spirit as the leading private Sri Lankan Bank.

Our financial performance coupled with the role we played as a leading socially responsible corporate citizen and a model employer, places us at the top of the corporate world in Sri Lanka. We have over the past decade delivered consistent and solid results and shown our resilience to operate in any circumstances. 2006 was no exception

and the Bank delivered value not just to its shareholders, but to the employees, customers, the wider community and the country as a whole.

## **The Bank continues to Grow**

In December 2006, we opened our 150th branch in Mahiyanganaya: a remarkable achievement for any financial institution. A total of 16 new branches were opened during the year. Our goal is to establish at least 10 new branches every year and last year we exceeded this target. Our operations in Bangladesh were strengthened by the addition of two new branches during

the year to bring the total number in that country to seven.

Our ATM network was also strengthened and we ended the year with 269 ATMs in Sri Lanka and 8 in Bangladesh.

We have begun to seriously focus on ease of access for customers to our delivery points. It is important that customers are able to access both branches and ATMs speedily and efficiently and so we have started relocating some ATMs with a view to providing greater convenience.



### Growing Internationally

The Bank's new Vision places a premium on having a strong international presence by 2011. We have already taken steps in this regard by investing in Bangladesh. We have made our mark there in a period of three years and for two consecutive years have been rated as the 'Best Foreign Bank' in that country.

We have been looking at the Indian market over the past several years. Sadly, the Indian regulatory environment is not favourable to foreign banks. We still face many hurdles if we are to establish a strong presence there, notably the challenge of raising substantial amounts of capital to set up operations. We will continue to explore every avenue with the idea of having a presence in India at the earliest possible opportunity.

Our presence in the Middle Eastern countries has gained momentum and we are upbeat about the prospects in those states. We have stationed Business Promotion Officers (BPOs) in Kuwait, Qatar and Bahrain, which facilitate the remittance of money from Sri Lankan expatriates based in those countries. While our presence is not in the form of full-scale banking operations, we anticipate upgrading the levels of our activities over the next few years and progressively establishing our brand in that region. BPOs will soon be

stationed in Oman and the UAE. In Italy and Canada we hope to open our own money remittance offices under the brand 'Commex'.

We appointed a BPO in Italy last year to tap into the Sri Lankan expatriate population estimated to be over 125,000, who is operating from the Rome Office of National Exchange Company (NEC). The Bank recently established an arrangement with NEC to remit monies to Sri Lanka using our own e-Exchange system. At present they have 21 offices covering the main towns in Italy, most of which have large pockets of Sri Lankan expatriates.

### Redefining Convenience

We will continue to expand our operations by investing in new infrastructure. We will accompany this with an enhanced focus on making our products more accessible and customer friendly. Not only are we making the branches and ATMs easier to access and use, but we are also progressively reducing the length and number of procedures that precede a transaction. Our goal is enhanced convenience and greater efficiencies all round.

The Bank rolled out a sophisticated cheque viewing facility for its customers last year. For the first time in Sri Lanka, Bank's customers can view images of cleared and paid

cheques issued by them, online, from their own homes and offices by merely clicking an icon on 'ComBank Online,' the Bank's Internet Banking system. All registered 'ComBank Online' customers can make use of this facility free of charge. Shortly, this facility will be extended to cheques deposited as well.

Our Visa Plus Debit, also launched last year, eliminates the need to carry cash. Unlike the credit card, the transaction amount is debited immediately to the customer's account. The Debit card can be used at more than 29 million locations worldwide, including 7,000 local merchants.

In 2005, the Bank launched COM-eLoad facility which allowed the mobile phone top-up facility to the Dialog KIT prepaid customers. Arrangements are being made to extend this facility to post paid customers for bills settlement.

FX Link, a capital guaranteed structured deposit product that was developed towards the latter part of 2006 will be launched shortly. This product will allow the investors the opportunity of earning a higher return by opening a simulated foreign currency trading account.

The Bank's Progressive Saver Account that was rebranded as the Power Saving Account in 2006 grew in popularity. This account enables the customers to receive a bonus interest of up to 100% on their deposit balances depending on the number of withdrawals.

The Bank continued to help industries through the E Friends - II Loan Scheme. The scheme can be used to purchase equipment that leads to a reduction of emission, improvement in safety at the workplace and reduction in the use of resources by existing equipment. Under this loan scheme the Bank also helps highly polluting industries to relocate to special estates that are equipped with special waste treatment plants.

There has been a tremendous response to ComLeap, our tiered savings scheme, since its inception in 2005. In order to make the product even more attractive, the Bank recently increased the interest rates, offering our customers an even better return on their deposits.

In 2006, the Bank tied up with MoneyGram, the global funds transfer company to enhance the Bank's e-Exchange money transfer system. The Bank now offers customers in over 104,000 locations in 170 countries, the ability to transfer funds over the Internet. These funds can be collected

on any day of the year through the Bank's holiday banking facility, which is now available in most parts of the country or from supermarket counters which are open till 7.30 p.m. everyday. The full amount remitted is paid and the beneficiary incurs no charges.

### **Pension 'Restructuring'**

In line with international best practices the Bank restructured its Pension scheme, under which employees will receive significant 'pay outs' at the time of separation. This pension 'restructuring' brings our terminal benefits policy in line with the rest of the global financial industry. The restructuring cost the Bank a hefty Rs. 1.654 billion in 2006 in terms of the provision required for the past service cost of employees who consented. Despite this, the Bank was able to deliver yet another stellar financial performance. A normalisation of the Bank's profits excluding the provision for the past service cost of restructured pension scheme would place the Bank far ahead of other local banks in terms of profitability.

The potential liability on the Bank's Pension Scheme which was a Defined Benefit Plan fluctuated widely, with funding deficits at times, depending on the movements in the actuarial assumptions such as the rate of interest and the rate of future salary increases. This restructuring resulted in the Pension Scheme being converted to a Defined Contribution Plan.

Each employee will receive a lump sum at the point of separation. Over ninety-nine per cent of our staff exercised the restructured option. We also built in other incentives to ensure that our staff remain with the organisation and do not seek to exit merely because of the substantial lump sum payment.

### **Upgrading the Risk Management Infrastructure**

During the year, we initiated a process towards the establishment of an integrated risk management department within the Bank. Commercial Bank, in consultancy with the Deutsche Bank, Asia Pacific Head Office, Singapore, unleashed a thorough process of review of our existing risk management practices. Our goal is to enhance the Bank's security through a prudent and efficient risk management strategy in partnership with an independent and capable outsider. The Bank hopes to commence implementation of the recommendations of the Deutsche Bank shortly.

### **Rationalising Our Investments**

In 2006, we disposed of our investment in the DFCC Bank for Rs. 1,909.259 million and realised a capital gain of Rs. 749.802 million.

### Exchange Rates Stabilise

After about two years of volatility, the exchange rates began to stabilise towards the latter part of 2006. In 2005, the Bank suffered considerably because of unforeseen exchange fluctuations due to the influx of foreign exchange after the tsunami causing the Rupee to appreciate considerably.

### Generating Profits in a High Tax Regime

One of the main challenges facing the banking industry in Sri Lanka is the inordinately high rate of taxation. Apart from increasing the corporate tax rate from 30% to 35% in 2006, the Financial VAT applicable to financial institutions too was increased to 20% from 15% with effect from January 1, 2006. The result is an effective tax rate of between 50%-60%, a disincentive to say the least, for any industry.

A balanced tax regime is urgently required if local banks are to grow, develop state-of-the-art products and expand into the regions. The current state of the industry in Sri Lanka calls for heavy financial outlays if existing infrastructure is to be upgraded and

IT capabilities are to be enhanced.

A tax regime that discourages such investment is going to stifle growth and be counter productive to the long-term interests of the industry and the country.

The Government's Budget proposals for last year envisage activating the 'Deemed Dividend Tax' in the Inland Revenue Act. Under this provision companies that do not pay out at least 25% of their distributable profits as dividends will be subject to the Deemed Dividend tax of 15% on the difference between one-third of the distributable profits and the actual dividends paid.

This proposal will have adverse consequences on the banking industry. Unlike other organisations, banks the world over are required to maintain capital commensurate with the level of risks undertaken. These requirements have been introduced by the respective regulatory bodies acting under the Basle Capital Adequacy Accords. Availability of adequate levels of capital reflects on the stability and financial soundness of a bank. 'Profits reinvested' is one of the primary sources of such capital and the proposed Deemed Dividend Tax will have a negative impact on the amount of profits that can be reinvested.

### Sustaining Profits in a Turbulent Environment

Our biggest challenge continues to be the external environment where both political and other factors have created a degree of turbulence. Inflation has begun to assume alarming levels and this will have an impact on all aspects of our operations. We trust the Central Bank will follow a prudent policy in this regard and be able to bring down the rate of inflation during the year.

The overall security situation continues to trouble not just the banking industry but the whole business community. The leisure industry, which we finance, has been particularly affected and so have a number of our other clients. We trust the Government will take steps to bring the security situation under control and divert the massive defence expenditure towards development needs.

The new provisioning policy of the Central Bank requires the banks to build up a general provision of one per cent on all performing and overdue loans on or before March 31, 2009. This requirement will pose a new challenge to the banking industry. Revenue Authorities do not

permit banks to treat general provisions as a deductible expense. In addition, the Sri Lanka Accounting Standards require that such general provisions be treated as appropriations.

Banks were required to maintain capital for Market Risk commencing from the first quarter of 2006. Capital Adequacy computation under the Basle II Accord from the first quarter of 2008 will require banks to maintain capital for Operational Risks as well. Risk weights applicable for mortgage lending and other loans and advances were increased from 50% to 55% and from 100% to 110% in the fourth quarter of 2006. All these exert pressure on the capital adequacy levels of banks.

These new policies regrettably, will translate into an increase in the cost of borrowing for the customers.

### **Banking Consolidation**

I am happy to note that the Central Bank has recently issued a policy direction on shareholder ownership and banking consolidation. The Bank has seen some tensions develop amongst its shareholders and received some adverse publicity as a result. In this respect, the Bank welcomes the policy direction provided by the Central Bank in January 2007.

According to this direction, no single shareholder will be permitted to hold more than 15% of issued share capital carrying voting rights. This limit will apply to acquisition or a holding of shares by all categories of shareholders, individuals and groups, whether acquired or held directly or indirectly or through a nominee or acting in concert with any other category of shareholders. In the case of licensed commercial banks, approval of the Monetary Board and the concurrence of the Hon. Minister of Finance are required to acquire shares carrying voting rights in excess of 10% of the issued capital.

### **Remarkable Consistency**

The Bank has managed to perform with remarkable consistency over the past ten years. It has continued to deliver value to all its stakeholders with aplomb and in varying social and political conditions. It is not just the financial performance that has been remarkable, but we have also built remarkable customer relationships, developed cutting edge products, generated an imaginative and dynamic human resource base and empowered marginalised communities.

I want to acknowledge here the continuing strength of our human resource pool. The staff, in every part of the country, has driven the Bank to

new heights through their innovation and commitment. Having taken the Bank to the top they now work to ensure we remain there. My thanks also go out to all those on the Board for their expert guidance and support. I wish to make special mention of the invaluable services rendered to the progress of the Bank by Mr. J.S. Mather during his tenure of service as a Director, the Deputy Chairman and the Chairman of the Audit Committee. I also wish to express my appreciation for the services rendered by Mr. Sanjiva Senanayake during his tenure of service as an Alternate Director. I appreciate the cooperation of the officers at all levels at the Central Bank of Sri Lanka.

I wish to thank Messrs. Ernst & Young for the professional approach in conducting the external audit and issuing the report on time, enabling the Bank to publish this Annual Report and to conduct the Annual General Meeting early.

I look forward to another remarkable and rewarding year.



**A.L. Gooneratne**  
*Managing Director*

Colombo  
February 15, 2007

## Corporate Management



### Corporate Management

**1 A.L. Gooneratne** (Managing Director) **2 G.L.H. Premaratne** (Senior Deputy General Manager - Corporate Banking) **3 R. Samaranyake** (Senior Deputy General Manager - Finance & Planning)  
**4 W.M.R.S. Dias** (Senior Deputy General Manager - Personal Banking) **5 G.L.C. Amarasiri** (Deputy General Manager - Human Resource Management) **6 B.H.M.G. Dharmasiri** (Deputy General Manager - Corporate Banking) **7 S.D. Bandaranayake** (Deputy General Manager - Operations) **8 M.A. Pemasiri** (Deputy General Manager - Services) **9 Delip Fernando** (Deputy General Manager - Inspection)  
**10 P.V. Ratnapala** (Asst. General Manager - Personal Banking I) **11 D.S. Weeratunga** (Head of Global Treasury) **12 K.D. Nimal Luxshman** (Asst. General Manager - Personal Banking II)  
**13 Jegan Durairatnam** (Asst. General Manager - International) **14 Mrs. Marion Abeywardena** (Asst. General Manager - Corporate Banking) **15 Dudeepa Ratwatte** (Head of Global Markets)

Absent: **M.D.A. Peiris** (Deputy General Manager - Information Technology)

### Senior Management

**16 S. Raghavan** (Head of Exports) **17 Vimal Fernando** (Senior Regional Manager - Colombo South) **18 Ajith Wijayasundara** (Head of Information Technology) **19 Mrs. Carmelita De Silva** (Head of Corporate Banking) **20 Chandana Gunasekera** (Senior Regional Manager - Colombo Inner) **21 Claude Perera** (Head of Human Resource Management) **22 Palitha Narangoda** (Market Risk Specialist)  
**23 Felician Perera** (Head of Recoveries) **24 Richard Rodrigo** (Head of Marketing) **25 Palitha Perera** (Head of Operations) **26 Mrs. Sandra Walgama** (Regional Manager - North Western)  
**27 C.M. Abeysekera** (Chief Manager - Corporate Banking) **28 Mrs. Sarojini Dunuwille** (Chief Manager - Legal) **29 S. Renganathan** (Country Manager - Bangladesh) **30 Hilary Fernando** (Chief Manager - Treasury Processing) **31 Niran De Costa** (Regional Manager - Colombo North) **32 B.W.R. Srikantha** (Regional Manager - Central) **33 Naveen Sooriyarachchi** (Chief Manager - Corporate Finance)  
**34 Duminda Kurukulasuriya** (Chief Manager - Imports) **35 Roshan Perera** (Regional Manager - Greater Colombo) **36 Mrs. R.R. Dunuwille** (Company Secretary) **37 Nugent Kapuwatte** (Chief Manager - Leasing and Personal Loans) **38 Noel Wickramasinghe** (Chief Manager - Logistics) **39 Lakshman Perera** (Chief Manager - Card Centre) **40 Anura Ratnayake** (Chief Manager - Operations - Foreign Branch)  
**41 V.S. Rajasooriyar** (Regional Manager - North Eastern) **42 Vajira Thotagammuna** (Chief Manager - IT Operations) **43 Sarath Pallewela** (Chief Manager - Security)



## Management Committee - Bangladesh



**1 S. Renganathan** (Country Manager) **2 D. Das Gupta** (General Manager) **3 S. Prabagar** (Chief Operating Officer)  
**4 S. Kutubuddin Ahmed** (General Manager - Risk, Compliance and Corporate Affairs) **5 Golam Mortuza** (Deputy General Manager - International Trade)



Chief Operating Officer - Bangladesh, receiving the "Best Foreign Bank" award for the second successive year at the Arthakantha Business Awards 2005", from the Minister of Health and Family Welfare, Bangladesh.



Commercial Bank also bagged the "Robintex - Financial Mirror - Partex Business Awards 2006". Country Manager - Bangladesh accepting the award from the Minister for Science and Information, Communication and Technology, Bangladesh.

# HIGH QUALITY BANKING RECORD LEVEL PROFITS

## Financial Review

In the year 2006 too, Commercial Bank was able to deliver strong performance and continue to be the most profitable and financially strong bank in Sri Lanka, among its peer banks, as evident from the profits discounting the exceptional items, financial ratios and the local and international recognition it has received.

Solid performance in most areas of business helped the Bank report a record level of earnings in 2006. Strong organic growth was seen in almost all major activities. Despite the customer base and the volumes of business recording substantial increases, the Bank managed to maintain a consistent risk profile and in fact reported improvements in credit quality in terms of non-performing assets ratio. Costs, discounting the provision made towards the cost of the restructured pension scheme, continued to remain firmly under control and the growth in earnings well exceeded the growth in costs. All these factors contributed to further strengthen the pre-eminent position of the Bank in the Sri Lankan banking industry.

However, since the Bank had to rely mainly on profit retention to support enhanced capital requirements arising from the assets growth, Capital Adequacy Ratios continued to be under pressure. It is widely believed that only a single digit growth in risk weighted assets can be supported with internally generated funds alone. In addition, the direction from the Central Bank towards the latter part of the year, requiring the banks to risk weight credit facilities granted against residential mortgages and other loans and advances at 55% and 110% respectively (as opposed to previous risk weights of 50% and 100% respectively) also exerted an added pressure on the ratios. However, as detailed in the Chairman's Review, the proposed rights issue of shares will improve the capital funds position and support future expansion of business.

During the year, the Board of Directors of the Bank having considered various adverse implications of the existing pension scheme of the Bank [which was a Defined Benefit Plan (DBP)], approved a restructured plan, designed by Hewitt Outsourcing Services (India) Ltd, aimed at converting the pension scheme that existed as at August 31,

2006, from a DBP to a Defined Contribution Plan (DCP). This restructured plan was offered on a voluntary basis to all the eligible employees during the fourth quarter of the year. The scheme provided for lump sum payments instead of pensions to the eligible employees at the point of their separation, in return for surrendering their pension rights. The lump sums offered consist of a past service package and a future service package.

The initial cost on account of the past service package in excess of the funds available in the Pension Fund which was Rs. 1.654 billion, was borne by the Bank. However, after adjusting for the saving on the Financial VAT, the net cost to the Bank was around Rs. 1.378 billion, only. The future service package includes monthly contributions to be made by the Bank for the employees who accepted the offer, during their remaining period of service, at pre-determined contribution rates to be applied on their salaries, estimated to increase for this purpose at 10% p.a. In addition, actual interest to be earned by the Pension Fund too would be allocated on a pro rata basis to the employees who joined the new scheme.

# TAKING THE MICKEY OUT OF THE MOUSE



The computer is today not just a machine of convenience. It is an energizer, friend, soul mate and entertainer. In a world where 'change' is a buzzword and a philosophy, we cling to some things classical, yet embrace human innovation with the passion of a lover. Another few steps up... the ladder of convenience.



With the implementation of the new scheme, the Bank would be able to prevent the future funding deficiencies in the Fund on account of the employees who accepted the offer. The Pension Fund had a funding deficit of Rs.1.321 billion, as per the last Actuarial Valuation done as at August 31, 2006.

The pre-tax profit of the Bank increased to Rs. 4,213.545 million after providing for Rs. 1.654 billion towards the restructured pension plan and the payment of Financial VAT of Rs. 970.958 million for the year ended December 31, 2006 as against a pre-tax profit of Rs. 3,641.960 million in 2005, recording a growth of 15.69%. Net income increased by 41.03% to reach Rs. 12.515 billion. The increase in net income was facilitated by a 30.46% growth in net interest income mainly due to growth in interest earning assets consequent to strong business momentum, 145.18% growth in foreign exchange profit mainly due to the translation gains earned on the profits retained in the Off-shore Banking Centre consequent to the depreciation of the Rupee against the US Dollar during the year by 5.37%, 14.30% growth in fees and commission income consequent to increased business volumes and other income by 106.83%. The substantial growth in the other income was mainly due to the profit earned by the Bank on the sale of the DFCC shares during the year. Operating expenses increased by 58.68%, mainly due to the provision made for the

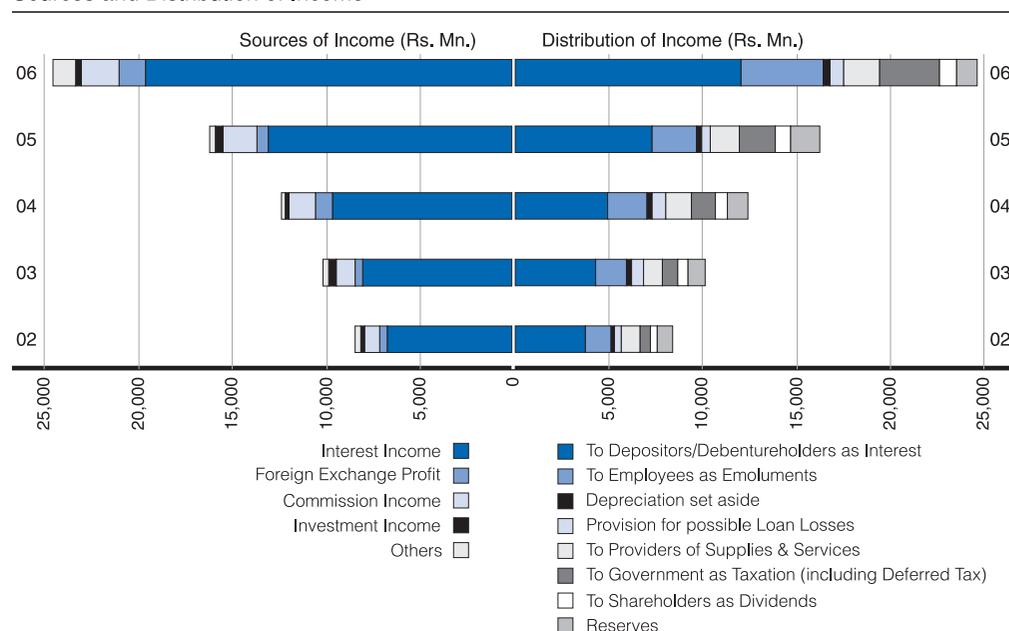
restructured pension scheme and the increase in the Financial VAT rate on profit to 20% in 2006 from 15% last year.

Although the Bank's pre-tax profit recorded a growth over 2005, its post-tax profit of Rs. 2,012.628 million in 2006 recorded a negative growth of 14.87% compared to the post-tax profit of Rs. 2,364.240 million reported in 2005. This was mainly due to the increase in the provision for taxation from Rs. 1,277.720 million to Rs. 2,200.917 million mainly as a result of the increase in the corporate tax rate to 35% in 2006 as against 30% last year, the contributions to the Pension Fund and the Employees' Provident Fund in excess of 25% of the salaries of the pensionable employees being disallowed for tax purposes and taxes

paid in Bangladesh on the profits repatriated from the Bangladesh operation during the year etc.

The provision for possible loan losses increased to Rs. 655.070 million in 2006 mainly due to additional general provision made on performing and overdue loans and advances portfolio as required by a recent direction from the Central Bank of Sri Lanka. However, consequent to this additional provision, the Provision Cover and the Open Credit Exposure Ratio of the Bank further improved to 60.41% and 8.61% respectively, as at December 31, 2006 from 53.85% and 12.37% as at December 31, 2005. In 2006, the Bank was able to reduce the non-performing assets ratio to 2.74% from 3.22% in 2005. This is considered to be the lowest among the peer banks based on the published

Sources and Distribution of Income



A close-up photograph of a hand holding a blue magnetic card, swiping it through a modern, gold-colored door lock mechanism. The hand is positioned on the right side of the frame, and the card is being inserted into a slot on the lock. The background is a plain, light-colored wall.

# DOORS WILL ALWAYS OPEN

The jangle may be less, but the convenience is more. In today's world the magnetic card swipes many more things open. Doors will always open if you push hard enough. Sometimes the push is physical but most often it is mental and imaginative. Open doors open new opportunities and new ideas. Another few steps up... the ladder of convenience.



financial statements up to September 30, 2006 and signifies a remarkable improvement in risk management, post-sanction monitoring and recovery efforts.

The Bank's Bangladesh operations continued to be very successful and repatriated a profit of US \$ 2.700 million, during the year.

Commercial Bank also had the largest market capitalisation, among all listed banks in Sri Lanka as at December 31, 2006 and ranked No. 5 among all listed companies on the Colombo Stock Exchange.

The Directors recommended a 35% final dividend payable on March 28, 2007, which together with the interim dividend of 15% paid in November 2006 will add up to a total dividend of 50% for the year 2006 on the issued share capital of the Bank.

The pre-tax profit of the Commercial Bank Group amounted to Rs 4,321.153 million as against Rs. 3,668.048 million recorded in 2005, which amounted to a growth of 17.81%.

The post-tax profit of the Group for the year which amounted to Rs. 2,072.402 million, reflected a drop of 12.11%, compared to the post-tax profit of Rs. 2,358.079 million, of the Group in 2005, mainly due to the reasons that led to a lower post-tax profits of the Bank, as explained earlier.

The Group continued to maintain key financial ratios at healthy levels, in comparison with industry standards. The Group reported a basic earnings per share of Rs. 13.12.

The business volumes of the Bank recorded impressive growths during the year. Deposits grew by 23.54% while loans and advances mirrored this trend recording a growth of 25.77%. Deposit mobilisation efforts of the Bank were supplemented by several issues of bonds and debentures. US \$ 10 million was raised by issuing a 5-year bond via a private placement, the first of its kind by an indigenous bank in Sri Lanka. Further, the Bank issued debentures worth Rs. 1.000 billion and Rs. 1.127 billion through a private placement in May 2006 and through a public issue in December 2006, respectively. Total assets of the Bank increased to Rs. 223.974 billion, as at December 31, 2006, as against Rs. 180.077 billion, reported as at December 31, 2005, recording a growth of Rs. 43.897 billion, or 24.38%.

It is interesting to note that the Bank has been able to maintain Compounded Annual Growth Rates in excess of 25.23%, 25.34% and 21.93% respectively in Deposits, Loans & Advances and Pre-Tax Profits over the past ten years.

The contribution made by the three broad business divisions viz. the Corporate Banking, the Personal Banking and the Treasury to the profits and business volumes of the Bank is summarised below:

	2006		2005	
	Rs. Mn.	%	Rs. Mn.	%
Profit before Tax:				
- Corporate Banking	<b>1,681.16</b>	<b>39.90</b>	1,635.09	44.90
- Personal Banking	<b>2,225.61</b>	<b>52.82</b>	1,760.38	48.34
- Treasury	<b>306.78</b>	<b>7.28</b>	246.49	6.76
<b>Total</b>	<b>4,213.55</b>	<b>100.00</b>	3,641.96	100.00
Loans and Advances (Gross):				
- Corporate Banking	<b>85,306.11</b>	<b>55.33</b>	69,148.75	56.67
- Personal Banking	<b>68,868.24</b>	<b>44.67</b>	52,881.66	43.33
<b>Total</b>	<b>154,174.35</b>	<b>100.00</b>	122,030.41	100.00
Deposits:				
- Corporate Banking	<b>40,851.41</b>	<b>25.92</b>	34,614.27	27.13
- Personal Banking	<b>116,782.66</b>	<b>74.08</b>	92,987.01	72.87
<b>Total</b>	<b>157,634.07</b>	<b>100.00</b>	127,601.28	100.00

The performance, major initiatives during 2006 and plans for the future of these three divisions are discussed in detail.

# VERTICAL LOCOMOTION



The thrill of the rise; the ecstasy of the fall. Going up is as heady as going down. The locomotion of a modern elevator is like the rhythm of human life: the ebb and the flow, the rise and fall, a smoother ride, a newer idea. It is the ride of supreme convenience. Another few steps up ... the ladder of convenience.



## CORPORATE BANKING

### Corporate Banking Products

- o Letters of Credit
- o Shipping and other guarantees
- o Import and export finance
- o SWIFT facilities
- o Syndicated loans
- o Project financing
- o Securitisations
- o Structuring, managing and underwriting of Initial Public Offerings and Private Placement of Equity
- o Company valuations and restructuring
- o Investment advice and evaluation
- o Structuring of Corporate Debt Instruments
- o Working capital financing
- o Internet banking
- o Sponsor of the Colombo Stock Exchange
- o Bullion trading
- o Domestic and International Factoring
- o Off-shore banking facilities
- o Leasing

### Core Competencies in Corporate Banking

- o Expertise in trade finance and corporate credit
- o High level of professionalism
- o Speedy response to customer requests
- o Customer friendly service
- o Innovative products
- o State-of-the-art technology
- o Largest linked branch network
- o Margin provider and underwriter for Capital Market Activities

### Future Strategies for Corporate Banking

- o To offer exclusive and the best service standards in the Industry
- o To strengthen and broaden our presence in Bangladesh
- o To consolidate relationships with Maldivian clients
- o To simplify operations and ensure speedy delivery
- o To offer the most competitive terms backed by state-of-the-art IT
- o To further improve the quality of the total advances portfolio.
- o To diversify the advances portfolio.
- o To leverage on the strong relationships with our worldwide correspondents.

### Overview

The Corporate Banking Division comprises of the Foreign Branch, the Corporate Finance Unit (CFU), the Off-Shore Banking Centre and the Bangladesh operations. This Division with its expertise in Trade Finance, Corporate Finance, Project Financing, Leasing, Factoring, Working Capital Financing and related services caters mainly to the banking needs of the large to medium size domestic corporate customers and multinational corporate clients.

### Achievements - 2006

#### Sri Lankan Operations

- Loans and advances granted recorded a healthy growth of 23.37%, despite uncertain political and economic environment that prevailed in the country during the year.
- The Foreign Branch recorded a growth of 31% to achieve a lease portfolio of approximately Rs. 2.100 billion as at December 31, 2006.
- Lending portfolio to the Maldivian corporate clients continued to grow satisfactorily. It is noteworthy to mention that the portfolio has been of high quality despite the Bank not being physically present in the Maldives.
- Turnover from domestic factoring business also recorded a growth of 12% to reach a level of Rs. 3,996.4 million, from Rs. 3,571.9 million in 2005. Turnover from the export factoring business that the Bank commenced in 2005 under the membership of the Factors Chain International reached US \$ 4.259 million, a remarkable growth compared to the turnover of US \$ 0.096 million for 2005.
- The CFU structured and managed the one and only IPO in Sri Lanka during the year, which is considered a significant achievement. The unstable political climate, the rising interest rates, the breakdown of the peace talks and the looming war situation in the country during the year 2006, were not very conducive for capital market activities. As such, the fee based income earned by the CFU was lower than that of the previous year.
- Sale of bonds warehoused by us was not however active despite our efforts to develop the secondary bond trading market, owing to the aforementioned reasons. However, we continued to invest in securitised bonds and debentures during the course of the year and hope to pursue on this goal of promoting secondary market bond trading in the year 2007.

# LICKED, STAMPED AND DELIVERED

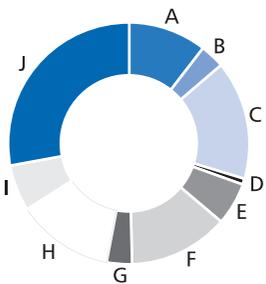


Instant communication: the dream of yesterday's visionary is the routine of today's persona. Instant responses, contemporaneous conversations, constant chat; what better stamp of modern convenience than 'electronic mail'. Another few steps up ... the ladder of convenience.



**Sectoral Classification of Loans & Advances - 2006**

A Exports - 11%	F Imports - 13%
B Tourism & Allied - 3%	G Consumption - 4%
C Industrial - 16%	H Services - 13%
D Agriculture & Fishing - 1%	I Housing & Construction - 6%
E Commercial Trading - 6%	J Others - 27%



- The CFU developed a unique revenue sharing loan product similar in some aspects to Islamic Banking products. The primary aim of this product is to fund eligible projects in a far more flexible manner than is customary. The main areas of flexibility are the repayment period, debt: equity requirements and the recovery of capital and interest in line with the cash flows of the project. It is anticipated that this product will be of benefit to start up projects with longer gestation periods.

**Bangladesh Operations**

- Deposits grew by 26.35% and Loans & Advances recorded a lower growth of 17.84%, in Taka, consolidating our position in Bangladesh further.
- Two more branches were opened at Sylhet and Uttara bringing the total number of branches and booths in Bangladesh to seven and increased the number of ATMs to 9 including 2 at off-site locations, reflecting our commitment to the country and exhibiting the desire to gradually move into Retail Banking.
- The number of “CAT” cards issued during the year exceeded 3,000.
- Agreement was signed with the Bangladesh Export Processing Zone Authority (BEPZA) to open a booth at its Chittagong premises with a view to provide better services and to facilitate the investors.
- Three new products were introduced namely, “High5FD”, a unique 5-year fixed deposit account, “Shamriddhi”, a tiered savings account designed to offer higher returns and “DotCom”, a savings account for teenagers.
- e-Banking Unit was set up offering settlement of payments through electronic transaction system, assistance in remittances from foreign countries, Internet Banking Services etc.
- Was adjudged as the “Best Foreign Bank” in Bangladesh at the “Arthakantha Business Award 2005”, for the second successive year.
- Was adjudged as the “Best Foreign Bank” in Bangladesh at the “Robintex - Financial Mirror – Partex Business Awards 2006”.



## GET SET, READY, GO

The joy of a turbo start, the fantasy of unceasing motion. The convenience of moving from Point A to Point B with the convenience of modern ignition. No hand crank, no aching shoulder. Another few steps up ... the ladder of convenience.



## PERSONAL BANKING

### Personal Banking Products

- o Current, Savings (Passbook and Statement) and Fixed Deposit Accounts
- o CAT Cards
- o Credit Cards
- o Debit Cards
- o "Arunalu" and "Isuru" Minors' Accounts
- o "DotCom" and "DotCom Spin" Teen Saver Accounts
- o Power Savings Accounts
- o Certificates of Deposit
- o Salary Remittance Package
- o "Nivahana" Housing Loans with Fixed and Floating Rates
- o "Pahan" Personal Loans with top-up facility
- o "ComShakthi" Leasing facility
- o "Diribala" Development Loans
- o e-Exchange - Money transfer facility
- o Holiday Banking Centres
- o Saturday Banking
- o Priority Banking
- o ComBank Online-Internet Banking
- o Telephone/SMS Banking
- o "Udara" Senior Citizens' Deposit Account
- o "FC Plus" - Foreign Currency Savings Account with high interest rates
- o DOLLARSMART - Foreign Currency Deposits in Bangladesh
- o Utility Bill payment service through ATM/Internet Bancassurance
- o Com-e-Load-mobile phones reload facility
- o Mobile ATM
- o Com-Leap - Tiered Savings Accounts

### Core Competencies in Personal Banking

- o "ComNet" computer linked branch and ATM network
- o State-of-the-art Information technology
- o Wide range of products
- o "One Stop" facilities
- o Speedy and friendly service

### Future Strategies for Personal Banking

- o To develop new low cost delivery channels
- o To adopt new customer relationship and segmentation techniques
- o To expand cross-selling
- o To develop new products tailor-made to specific market segments

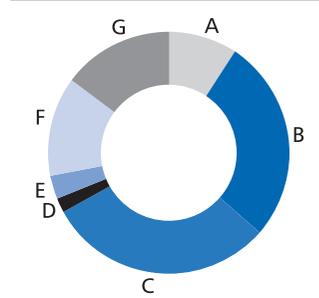
### Overview

The Personal Banking Division is responsible for the following activities:

- Successful operation of the extensive islandwide network of delivery channels which caters mainly to the banking needs of personal customers and small & medium enterprises.
- The eight Regional Offices which make an important contribution to the excellent performance of this Division by decentralising and expediting the process of decision making relating to credit and operations of Branches.
- Issue of "CAT" ATM cards and Credit & Debit cards under franchises from Master Card International and Visa.
- The operations of the Priority Banking Centre at the Reid Avenue branch that offers an array of exclusive benefits and privileges to its customers, befitting their special status and standing.
- Channelling low cost funds mobilised in excess of the lending requirements of this Division to the Corporate Banking Division and the Treasury for their lending and investment activities.

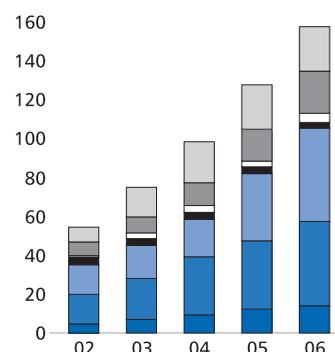
### Deposit Mix - 2006

- A Current Accounts - LKR - 9%
- B Savings Deposits - LKR - 27%
- C Time Deposits - LKR - 30%
- D Certificates of Deposit - LKR - 2%
- E Current Accounts - FCY - 3%
- F Savings Deposits - FCY - 14%
- G Time Deposits - FCY - 15%



### Growth in Deposit Mix (Rs. Mn.)

- Current Accounts - LKR
- Savings Deposits - LKR
- Time Deposits - LKR
- Certificates of Deposit - LKR
- Current Accounts - FCY
- Savings Deposits - FCY
- Time Deposits - FCY



### Achievements - 2006

- Sixteen new delivery points were opened and 46 ATMs were installed in Sri Lanka, including 5 at off-site locations, widening the network and making Commercial Bank truly a National Bank.

Delivery Points opened during the year consisted of 10 branches at Neluwa, Chavakachcheri, Warakapola, Udugama, Athurugiriya, Raddolugama, Kahawatte, Karapitiya, Welimada and Mahiyanganaya, 3 Customer Service Points (CSPs) at Jaffna, Boralesgamuwa and Delkanda, 2 MiniComs at Akurana and Beruwala and a Service Point at Kundasale increasing the number of delivery points in the network to 150 comprising of 125 branches, 7 CSPs, 17 Supermarket outlets and a Counter at the Bandaranaike International Airport and 269 ATMs. Bank considers this network, branded ComNet, to be a great asset that provides immense potential and opportunities for future growth of the Bank.

- CSPs at Pitakotte and Negombo were upgraded to fully-fledged branches.
- Branches at Kandana and Kirulapone were relocated in more convenient locations.
- Ampara and Galle City branches commenced 365-day banking while Kiribathgoda, Borella and Raddolugama branches commenced offering Saturday Banking.
- Substantial increase in the number of transactions through the ATMs, which dispense on average Rs. 178 million in 42,000 transactions each day, bears ample testimony to the immense popularity of our “CAT” ATM network.
- The number of “CAT”/Debit cards issued during the year alone exceeded 250,000, leading to the total number of cards issued, to exceed 1,250,000.
- Introduction of Visa Debit cards .

## TREASURY

### Treasury Products

- o Foreign exchange dealings
- o Forward exchange bookings
- o Commercial Paper
- o Foreign currency swaps
- o Interest rate swaps
- o Advice on foreign currency market movements

### Core Competencies in Treasury

- o Expertise on foreign currency movements and asset management
- o Expertise on foreign currency related products development

### Future Strategies for Treasury

- o Developing innovative treasury products
- o Streamlining risk management measures
- o Developing fee based operations through debt market instruments

### Overview

The Treasury is primarily responsible for the following activities:

Managing the liquidity, exchange positions and exposure to market risks and mobilising resources from domestic as well as international markets.

Achieving preferred balance sheet mix and maximising the returns therefrom whilst minimising the risk to the Bank.

### Trends - 2006

Local currency came under intense pressure and traded in volatile ranges with inflation and money supply growth galloping ahead at an alarming pace. However, growth numbers issued by the Central Bank of Sri Lanka showed definite improvements with favourable predictions for the future.

The Rupee depreciated by 5.37% on the back of political uncertainty, resurgence of violence, rising global oil prices and the high level of inflation.

Inflationary pressure also showed no signs of easing, fuelled by higher credit growth and the reluctance of the authorities to tighten interest rates at a much faster rate. This resulted in the country having negative real interest rates in 2006.

The interest rates in the United States were seen to be stabilising after prolonged rate increases to combat inflation, whilst the US Dollar lost ground against most major currencies. GBP, EUR and AUD appreciated against the greenback on yield advantages with these countries increasing rates in 2006 and hinting of further hikes if inflation persisted.

### Achievements - 2006

- Managed an asset portfolio of Rs. 39.537 billion as at December 31, 2006 as against Rs. 39.694 billion a year before.
- Made a contribution of Rs. 306.782 million to the profit before tax of the Bank while maintaining a substantially good transfer price to the branches and other business units.
- Structured a US Dollar denominated bond via a private placement with a tenor of 5 years.
- Raised Rs. 1.000 billion and Rs. 1.127 billion via a private placement and through a public issue of debentures respectively.
- Restructured the Treasury Division which now comprises of the Foreign Exchange Desk, the Assets and Liability Management (ALM) Desk, the Money Market Desk, the Fixed Income Securities (FIS) Desk and the Structured Products Desk.

- Operations of the Treasury front office were streamlined according to its product lines, to create profit centres within the Treasury Division and to cater to customer needs even better. The argument for this was to have a structure which will improve the level of efficiency and accountability of the traders/dealers. This move is keeping in line with most international banks.
- The Foreign Exchange Desk which comprises of sales and inter-bank trading saw substantial growth in business volumes and exchange profits improved by 33%, from 2005. It was extremely active in the local spot and forward markets and also in G-7 currency markets during the year and contributed substantially to the profitability of the Treasury.
- An independent unit has been set up to monitor Market Risk apart from the Treasury front office and Treasury Processing Department.
- Committed to providing a wide range of products to our clients, a new Structured Products Desk has been created. This desk has been instrumental in hedging US Dollar 20 million of Dollar denominated Sri Lankan Government Bonds in 2006.
- The Fixed Income Securities Desk continued to perform admirably achieving 80% of the budgeted profits when most market players found it difficult during the year to come out of the red.
- The Treasury sales team mapped out an active sales plan with the aim of increasing market share and it was possible to forge ahead some significant new relationships during the year.
- The Bank procured a suit of software modules from IPS Sendero on ALM, Funds Transfer Pricing (FTP) and Profitability.
- The Treasury along with the Risk Management Department implemented the modules on ALM and FTP which are being tested.

## Information Technology

It was a year of consolidation for IT with the major task for 2006 being the completion of the “Hot Backup” - Disaster Recovery solution. Several “Role Swap” operations were carried out to confirm its effectiveness and more such operations would continue to be carried out at regular intervals to ensure the functionality of the Backup machine. Along with this, a comprehensive IT Disaster Recovery Centre was established. The IT Disaster Recovery Plan was suitably updated incorporating the functioning of the IT Disaster Recovery Centre.

The Bank’s expanding network “COMNET” was functionally improved with the introduction of network performance and monitoring tools, to ensure that it provides peak performance to the benefit of the customers.

Significant functional improvements were carried out to e-Banking products of the Bank, such as Internet Banking and e-Exchange during the year.

The IT security environment was further strengthened with the introduction and implementation of best practices and policies.

The main computer system availability continued to be high, at over 99%.

The Bank continues to have one of the largest computer networks in the country with a total of 150 branches/ service points and 269 ATMs as at end of 2006.

## Strategic Direction and the Challenges of the Bank

At a strategic planning residential workshop held in October 2006 on the theme of “Quantum Leap 2007 and Beyond”, the Corporate and Senior Management of the Bank reflected on the achievements of the Bank so far and deliberated extensively on the Vision, Mission and the strategic direction for the Bank. The Corporate Plan and the Budget for 2007-2011, prepared on the basis of the deliberations and the strategies agreed was approved by the Board of Directors in December 2006. This Corporate Plan and the Budget incorporates highly ambitious targets for the plan period together with specific time frames. The Corporate Plan and the Budget has immensely contributed in building up the target driven culture across the Bank and has helped the Bank in recording superior performance year after year and maintain its pre-eminent position.

The challenges that the Bank will have to face in pursuing the above strategic direction also have been identified, some of which are increasing competition and resulting pressures on interest margins, ensuring that the capital keeps pace

with the projected growth in business volumes to maintain Tier I and Tier I & II Capital Adequacy Ratios at comfortable levels, tax planning, proposed Deemed Dividend Tax and the requirement to make general provisions on performing and overdue loans, containment of costs in the wake of inflationary pressures, maintaining competitive edge in IT supremacy, managing exchange rate volatility, making the Bank Basle II compliant and enhancing the Bank’s capacities and processes to support faster growth and increases in direct and indirect tax rates.

Priorities identified in the Corporate Plan to be implemented in the medium term:

- Enhancing international presence as envisaged in the Vision of the Bank, thereby reducing the overdependence on the Sri Lankan economy further.
- Consolidation of the Bangladesh Operations by opening more branches and expanding the ATM network.
- Expanding export factoring and commencing import factoring.
- Expanding the remittance business further in the Middle Eastern countries.
- Setting up remittance business in several selected European countries, in Canada and in Australia, under the brand name “Commex”.

- Improving the risk management infrastructure.
- Improving key performance ratios.
- Promoting the Bank's subsidiary companies – especially ONEzero Co. Ltd. and X-pertise Ltd.
- Expanding credit and support services to the SME sector.
- Increasing the contribution from fee based operations.
- Making the maximum use of the distribution network.
- Offering the most competitive terms and the best service standards.
- Simplifying operations to ensure speedy delivery.
- Improving the quality of assets portfolio.
- Leveraging the relationships with the correspondent banks.
- Growth through business acquisitions.

The Bank has set its eyes on getting itself elevated from its current position of being the largest private bank in the country and will be working hard to get the credit rating upgraded.

### Sources and Distribution of Income

For the year ended December 31,	2006	2005	2004	2003	2002
	Rs. Mn.	Rs. Mn.	Rs. Mn.	Rs. Mn.	Rs. Mn.
<b>Sources of Income</b>					
Interest Income	19,532	13,033	9,584	7,931	6,613
Foreign Exchange Profit	1,439	587	874	397	464
Commission Income	2,011	1,760	1,377	1,051	824
Investment Income	305	441	217	401	179
Others	1,182	279	238	279	284
	<b>24,469</b>	<b>16,100</b>	<b>12,290</b>	<b>10,059</b>	<b>8,364</b>
<b>Distribution of Income</b>					
To Depositors/					
Debentureholders as Interest	11,955	7,226	4,878	4,218	3,747
To Employees as Emoluments	4,374	2,364	2,132	1,697	1,312
Depreciation set aside	376	299	260	222	200
Provision for possible Loan Losses	655	415	699	623	402
To Providers of Supplies & Services	1,919	1,527	1,373	1,069	920
To Governments as Taxation					
(Including Deferred Tax)	3,178	1,905	1,264	753	579
-Income Tax	2,201	1,278	819	477	321
-National Security Levy	-	-	-	-	257
-Debits Tax	6	4	4	4	1
-Financial Value Added Tax	971	623	441	272	-
To Shareholders as Dividends	911	869	650	538	327
To Reserves	1,101	1,495	1,034	939	877
	<b>24,469</b>	<b>16,100</b>	<b>12,290</b>	<b>10,059</b>	<b>8,364</b>



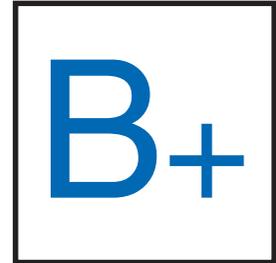
# Corporate Responsibility Rating

## Commercial Bank of Ceylon Ltd.

Analyst : Det Norske Veritas

Rating Scale: A+, A, A-, B+, B, B-, C+, C, C-, D

Date: February 9, 2007



### DNV's APPROACH

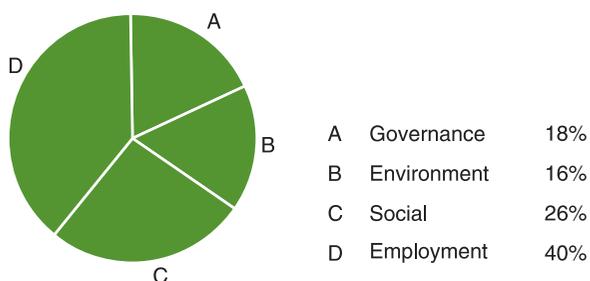
A Corporate Responsibility (CR) Risk Mapping outlining the main business conduct, environmental, social and employment risks for the Bank was undertaken. Using our proprietary methodology the identified risks were mapped against their potential to affect defined value drivers:

- Brand and reputation
- Regulation and litigation
- Human capital
- Operational efficiency
- Access to markets

The rationale behind our methodology is to provide an estimate of the potential effect on the value of Commercial Bank that individually identified impact areas may have. This means each impact area is weighted according to its likelihood to effect value; risks with high potential value impacts are weighted more highly than others making the need for a proactive management approach apparent.

Following the Risk Mapping, the quality of the management approach to each risk area is assessed and an overall rating on a scale of A+ to D is given.

**Weighting of Risk Categories**



### RISK ASSESSMENT

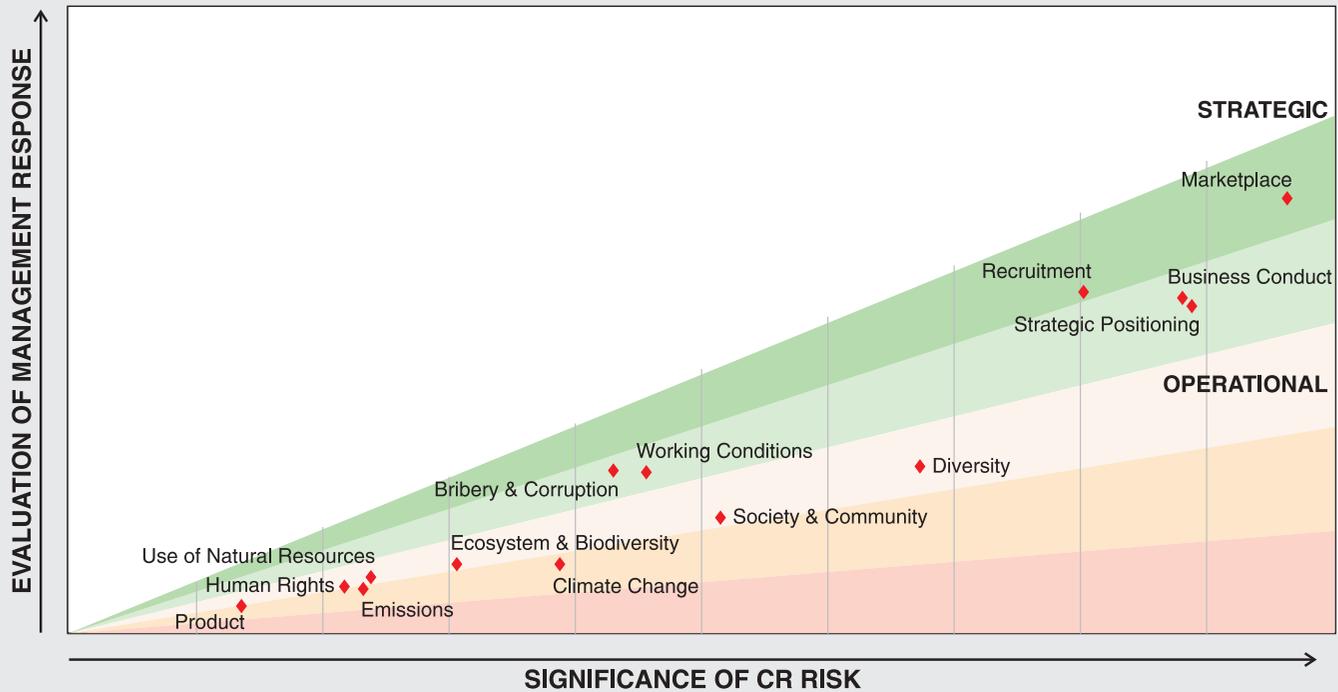
Our assessment shows that the majority of Commercial Bank's exposure to CR related risks relate to direct impacts that lie within the Bank's boundaries. The main direct impacts derive from its banking operations in their entirety. The Bank has direct influence over its employment policies, the provision of services and its business conduct. These impacts all have a significant potential to affect the reputation of the Bank, its competitive advantage and its operational efficiency.

### RATING SUMMARY

The Bank has identified most of its significant CR risks and is starting to actively manage them at a corporate level. Key risks relating to market-place, business conduct and human resources are all being individually managed as a matter of good business practice. These key risk areas all have strong policy definition and awareness throughout the organisation.

Commercial Bank is a signatory to the UN Global Compact. This internationally recognised set of principles is a suitable vehicle for a company of Commercial Bank's size to use as an overarching policy for the management of CR risks. However, despite awareness of the UN Global Compact being raised through internal publications, interviews within the organisation indicated that attentiveness to the existence of the UN Global Compact and how key areas such as credit policy could be used to address the aspirations of the UN Global Compact do not appear to have been explicitly made.

Commercial Bank has itself identified that it could lose potential business opportunities if it fails to properly evaluate situations with consideration for non-financial aspects. This is the key to strategic consideration of CR and the realisation that decisions

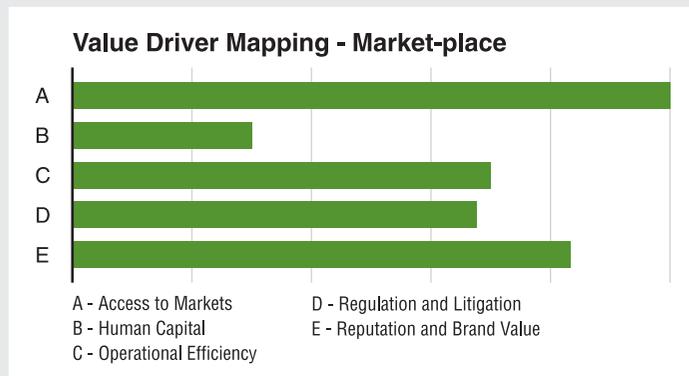


sometimes need to be taken from a medium to long term viewpoint.

By closing gaps in verification and assurance mechanisms, benchmarking against best practices, the setting of clear objectives and targets, and undertaking stakeholder disclosure in line with best practices Commercial Bank will be able to further embed CR into its overarching strategy and business practice.

**IMPACT AREAS AND MANAGEMENT EVALUATION**

**Market-place**



**Outline of risk**

The market-place can be sensitive to a number of issues relating to mis-selling (client information), responsible lending and marketing. Customer service provision through access to

branches, suitability of products and monitoring and complaint resolution procedures is also key to the market-place.

**Evaluation of management response**

Whilst no explicit policies addressing market-place risks are evident, Commercial Bank’s approach to such issues is enconced within its Vision statement “To be the preferred financial services organization in Sri Lanka, having an international presence by the year 2011” which will require a sound approach to the risks identified above. The Bank’s Code of Ethics further identifies the requirements for sensitive use of client information and the importance of communication. Whilst unwritten, interviews confirmed that the Bank’s policy towards marketing is one of caution and prudence, limiting the potential for mis-selling. The thorough training programmes that are evident within the Bank equip personnel with the knowledge and understanding of the Bank’s products.

Complaint resolution mechanisms for customers are in place. It is the nature of Sri Lanka that complaints are often made to senior personnel within a company, and Commercial Bank does not appear to be an exception to this rule. Complaints received in this manner are reportedly responded to within three days. In addition to the emphasis placed on employees to conduct business in an ethical manner, customer data is protected by IT security although elements such as conducting regular Ethical Hacking could be considered.

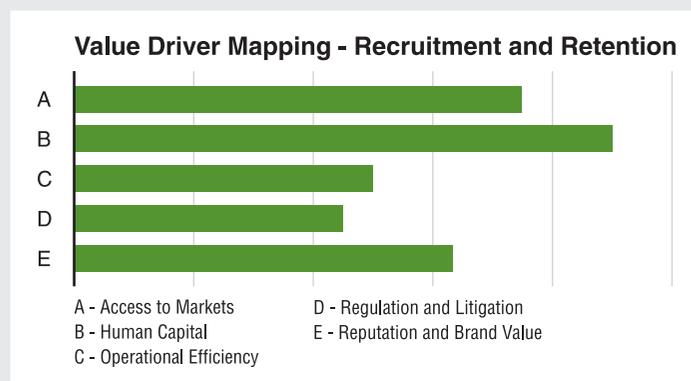


Every three years a customer feedback survey is completed, the next is due in 2007. The results of these surveys are generally favourable. A key outcome of the last survey identified the perception that staff was not too friendly. As a result, training programmes were changed to incorporate the need to put a “human face” on the Bank’s activity.

Market risks are currently identified within the internal risk register and as such are subject to the internal compliance process.

The Bank discloses its tariff systems on its website and as a matter of course when taking new accounts. Disclosure and KPIs regarding other issues such as level and nature of complaints, timeliness of response etc. are not readily available or regularly monitored by the Bank.

**Recruitment and Retention**



**Outline of risk**

Positioning of business as employer of choice through attractive contractual agreements on remuneration, on-the-job training & development, employee participation in decision-making, lack of transparency in remuneration systems, incentive structures, brain drain: loss of business/knowledge through loss of key personnel.

**Evaluation of management response**

Commercial Bank clearly recognises that its employees are its main asset. As such there is a comprehensive suite of policies and procedures in place to identify, recruit and through taking a market leading approach, retain its employees. These policies

and procedures are found in a combination of the employee guide book and the collective agreement.

Recruitment at the bank tends to be through its ‘trainee’ schemes whereby school leavers and business graduates are taken into the Bank and progress through a one to three year course combining educational and vocational processes. Discussions with the Bank indicated that it receives approximately 15,000 applications for c. 200 positions made available every year. As such, career progression is subject to a well defined policy and procedure, clearly mapping progression through competence based criteria. In terms of remuneration it is the Bank’s policy that all salary grades should be pegged to the 75th percentile with an aggressive variable pay element. Other benefits are all at levels dictated by legislation as a minimum. In many cases these are higher than legislative requirements, representing Commercial Bank’s position as the leading local bank.

Other training appears well structured and defined training programmes are in place for different grades (trainee, junior executive, executive, senior executive) whereby requisite procedural and technical knowledge is delivered approximately three times per year to those newly promoted to a higher grade. The frequency and availability of refresher training is not as apparent.

Whilst no defined CR training is delivered, CR related articles are a regular feature within the Bank newsletter “COM Pulse” which ensure a level of awareness amongst employees.

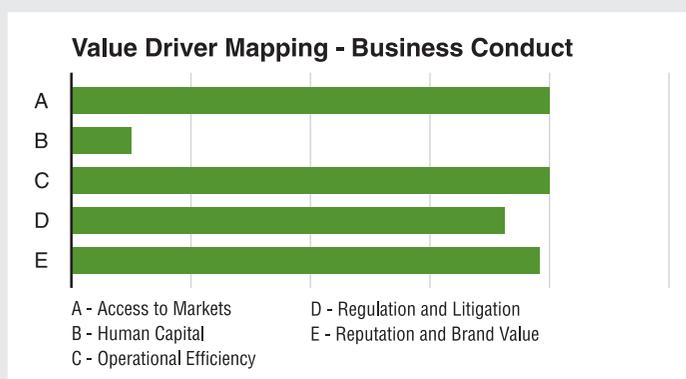
Commercial Bank currently employs 3,415 at the end of 2006, which is predicted to rise by 1,000 by 2011. The bulk of this growth will occur at the junior ‘entry’ level positions further enhancing the need for the Bank to continue its current recruitment and retention practices. Turnover is considered to be lower than the industry average, further demonstrating Commercial Bank’s apparent commitment towards its employees.

Aspects of HR are currently included in the risk register, particularly skills development and turnover rates and as such programmes in place to address these issues form part of the internal compliance framework.



There is limited disclosure in external reporting with regard to certain employee KPIs such as gender diversity but in terms of internal transparency it is clear that employment policies and processes are clearly communicated by the HR department with requisite checks and balances.

### Business Conduct



#### Outline of risk

Impacts associated with the industry concern business practices including, potential conflicts of interest, biased credit assessment procedures, abusive commercial practices, fair competition and insider and market time trading. As a company increases its global presence, employees are exposed to differing business practices that can compromise the integrity of a company or an individual. Anti-money laundering legislation is now a feature of the global financial markets.

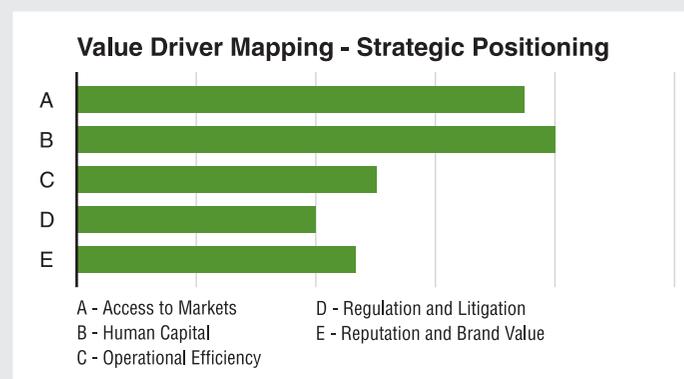
#### Evaluation of management response

In terms of policies addressing this impact area, Commercial Bank has a disclosed code of ethics which, although not benchmarked against international standards, addresses all key issues. The Code is comprehensive in nature and, as well as outlining the Bank's key policies, it provides context around the issues and also takes the reader through a number of case studies and examples of potential situations that may arise. This is considered to be an example of good practice. Through interviews it is apparent that business conduct is seen as a key factor in the maintenance of Commercial Bank's brand and as such is focused on and reinforced at every opportunity through a zero tolerance approach.

The expectation on employees is communicated at the commencement of employment and employees at various levels perform annual 'sign-off' of business conduct as part of the internal compliance framework. At the lending officer level a certificate of assurance is required and these cascade up to the senior management level and a requirement for a certificate of propriety to be completed annually.

Figures are available for the number of employees terminated for having breached the Bank's standards. Best practice in disclosure is to disclose the number of employees found to have breached Company standards and also to make estimates of the amount of business turned down by the Bank due to business ethics concerns.

### Strategic Positioning



#### Outline of risk

Procedures for managing major restructuring, branch closures, and termination of employment, collective bargaining, engagement in high-level dialogue on long-term strategic staffing issues including training to address long-term skills gap and staff demographics.

#### Evaluation of management response

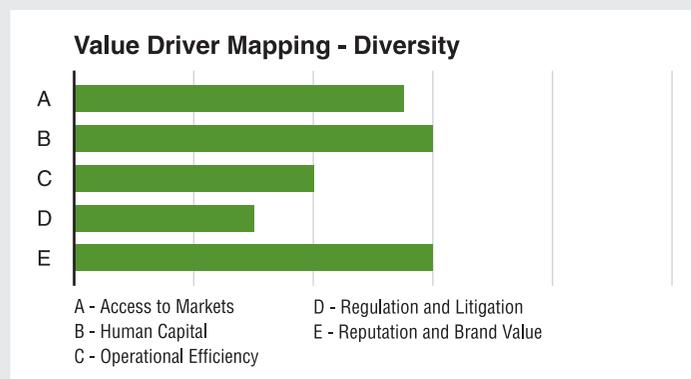
Commercial Bank has almost 100% employee representation, the majority of which is through the Ceylon Bank Employees Union (CBEU). Although it should be noted that no discussion with employee representatives took place in the scope of this assessment, the management of Commercial Bank considers itself



to have excellent relationships with union organisations. To illustrate this, Commercial Bank quotes the fact that it signed its most recent Collective Agreement with the CBEU one full day before the previous agreement expired. Reportedly, this is the first such time that this has occurred in the country's banking sector.

There is one nominated union representative at each branch, and monthly forums are held with employee representatives. During 2006, the Bank underwent a major restructuring of its pension scheme and it is apparent that this was conducted in a frank and open manner with ample communication, involvement of the employees and opportunities to feedback into the process. The Bank is aware of its need to address a potential gap in its senior grades for 2011 and as such commenced a programme of 360 degree feedback for approximately 30 individuals during the year. It is intended to extend the scope of this programme to include more employees with a view to determining a clear succession planning process for key positions.

**Diversity**



**Outline of risk**

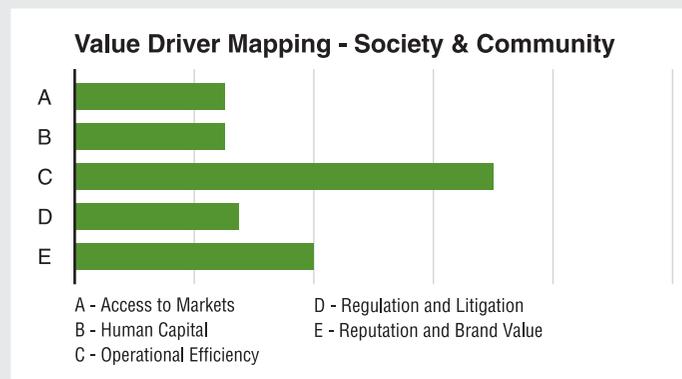
Equal opportunities, discrimination in recruitment, promotion and dismissal; beyond traditional areas of gender, race and disability, increasing focus on religion, age, sexuality, family rights, HIV/AIDS. Diversity a key driver in servicing minority segments of society.

**Evaluation of management response**

The employee guide book explicitly addresses discrimination on the grounds of ethnicity, gender, religious or political opinion, language, caste, age or disability. It is not apparent what systems and checks are in place to ensure that this policy is implemented. There is no evidence that the diversity statement is actively followed or monitored in the recruitment and promotion of bank employees.

Publicly available disclosure on the diversity of Commercial Bank employees is limited to age only in the current annual report. Commercial Bank works with the Employers' Federation to obtain the services of physically challenged persons and approximately 8%-9% of its workforce is Tamil. This figure is proportionate to the population of Tamils within Sri Lanka. Female employees represent 27% of the total although this proportion reduces towards senior management positions.

**Society and Community**



**Outline of risk**

A substantial proportion of the population, particularly in rural areas, do not use or have access to basic financial services. This can be due to a variety of reasons such as distrust of banks, poor credit histories or lack of financial awareness. Therefore access to products (branch network, customer and credit discrimination) and financial/debt management education are key areas to address. Tailoring of products and services for community groups e.g. low monthly deposits and retail-based



micro finance for individuals/SMEs are increasingly seen as a necessity. Indirectly, through lending activities, impacts on the community can arise.

**Evaluation of management response**

There is no evidence of any policies in place that address the Bank’s impact in the community. The Bank invests in community development programmes but this appears to be driven by government directives/expectations and tax saving benefits. There seems to be no formal system of identifying community needs and responding to them. In most of the cases, the Bank’s initiatives are based on requests from government and ‘philanthropy’ rather than ‘corporate responsibility’. This is by no means intended to detract from the actual philanthropic activities themselves which are beneficial to society and have made an impact for the communities involved.

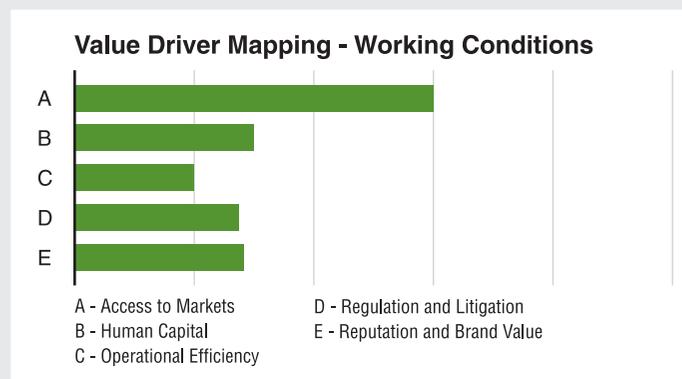
Regarding access to financial services for the wider populace, Commercial Bank can be seen to be very proactive in its expansion strategy. Whilst the business case for opening new branches is most prevalent in justifying the expansion policy the Bank can also be seen to be opening up access to banking services in areas of Sri Lanka outside of the traditional strongholds of Colombo and South-West of the country which is beneficial to the economy as a whole. This, combined with policies such as supermarket and holiday banking enhance access to services whilst simultaneously enhancing the Bank’s brand and market penetration.

Whilst a systematic process by which new products are determined and taken to market did not appear to be in place, it is evident that a ‘bottom-up’ approach is taken towards servicing the needs of customers. Interviews confirmed that initiatives or potential new products are identified by branches that have the knowledge of their local clientele, and subsequently fed through the management chain to determine their suitability. Examples of increasing the accessibility to savings can be seen through savings products that can be commenced with as little as Rs.100/- or child saving accounts that require no minimum or

regular deposits. In recognition of this approach, anecdotal evidence tends to suggest that competitors often follow Commercial Bank’s lead in these areas.

Commercial Bank’s credit policy contains the objective to serve the legitimate credit needs of the community and to support the development efforts of the Government. There was little evidence provided as to how these aims are systematically addressed within the lending activities of the Bank although there is evidence of support for directed lending programmes.

**Working Conditions**



**Outline of risk**

Office-based impacts - occupational health: small lifting operations, ergonomics, Repetitive Strain Injury (RSI), work/life balance, employee conduct and monitoring, stress related illnesses and long working hours are more of a risk in the corporate banking segment. Also potential target of terrorism and robberies making employee security a concern.

**Evaluation of management response**

A Health, Safety and Security policy reflects the Bank’s broader statements on safety issues and security addressed in the employee guide book. It is not clear how the implementation of this policy is monitored but an occupational health unit within the Bank provides various programmes such as counselling services and stress management programmes for branch managers. Other issues such as ergonomics are addressed in order to comply with legislative requirements.

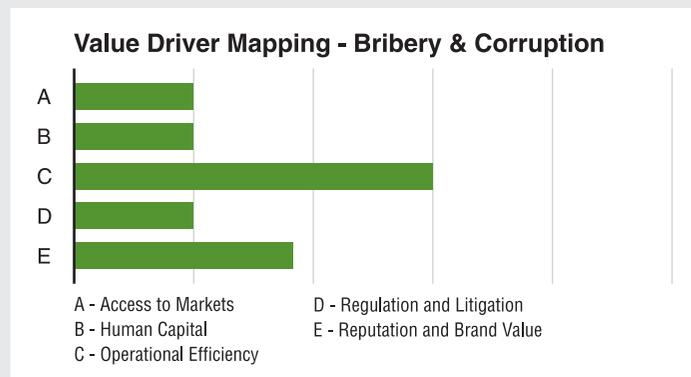


Grievance procedures are clearly defined within the collective agreements and as with all companies of a similar size and nature there are some cases passing through the grievance and tribunal procedures. It appears as if all employees are subject to due process and that procedures are followed.

The Bank has a policy of branch rotation, where for a number of business reasons, employees are expected to be transferred to different branches every five years. There is scope within the transfer policy for concessions and every effort to balance corporate versus individual needs is made. Relevant allowances and support structures are put in place for certain branch locations which are classified to identify difficult stations. This classification typically takes into account proximity to schooling and medical facilities amongst other things.

Employee surveys are conducted regularly and the last survey focused on commitment and received a 90% response rate. The findings from this survey were incorporated into the last round of strategic planning by the HR department. Disclosure surrounding working conditions is limited compared to what can be considered good practice. For example, similar organisations often report headline data from employee surveys as quantified evidence of employee policies and processes.

### Bribery & Corruption



#### Outline of risk

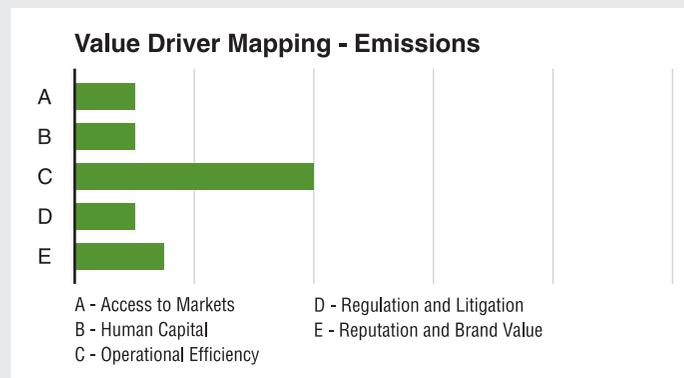
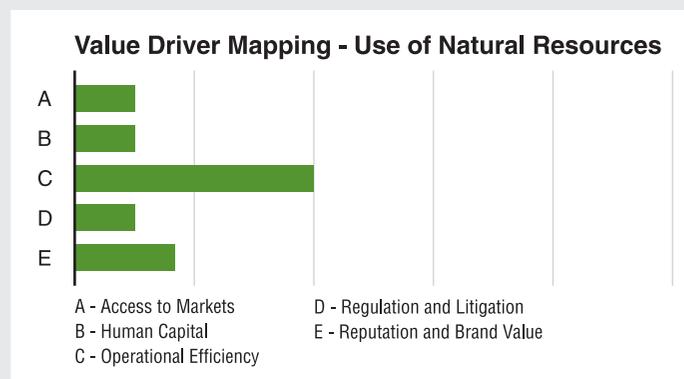
As a company increases its global presence, employees become exposed to differing business practices that can compromise the integrity of a company or an individual. The finance sector is ranked

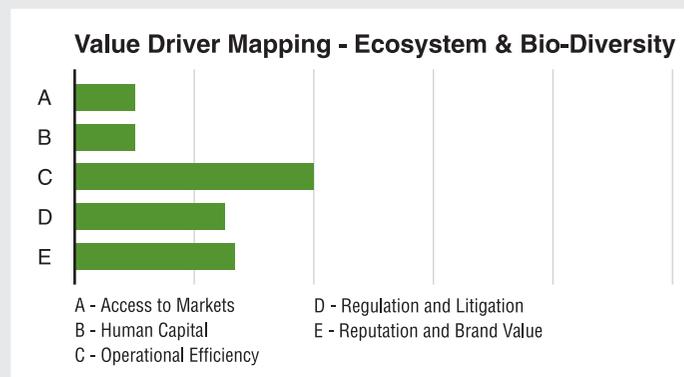
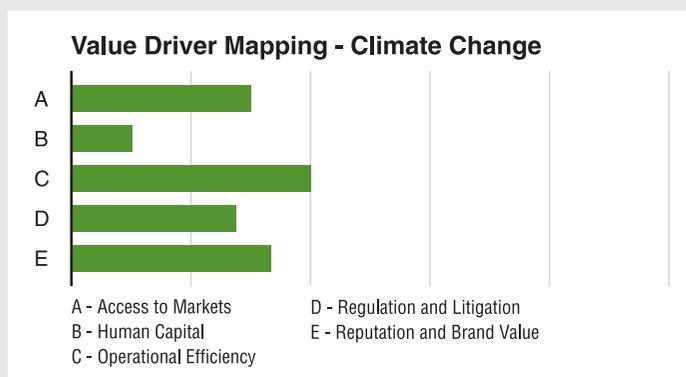
11 out of a list of 17 industries which are most likely to involve the payment of bribes in order to secure contracts according to Transparency International's (TI) 'Bribery Payers' Index.

#### Evaluation of management response

Commercial Bank's approach to business integrity and ethics is well enshrined in the day-to-day operations. Recently, particular emphasis can be seen to have been applied to the issue of money laundering due to recent regulatory changes. Guidelines on money laundering have been rolled out across all staff and various other controls are in place such as a limit on the value of transactions individuals are allowed to handle without permission from the line management. Reportedly, incidences reported to the ombudsman are rare and number less than three per year.

### Environmental Impacts





**Outline of risk**

Office-based organisations generate significant amounts of waste and consume large quantities of natural resources, particularly energy, water and paper. These can be influenced through daily operational practices and strategically through the choice and design of new premises. Indirectly, environmental impacts and risks arise through lending activities, such as corporate, project and export financing. Environmental issues can increase the level of operational risk on a credit operation, particularly in high impact or heavily regulated sectors.

**Evaluation of management response**

Direct impacts of normal working capital financing on the environment are limited and as such, Commercial Bank’s policies relating to the environment apply mainly to project lending propositions. There are some activities taking place where the Bank has identified its impact and is looking to minimise its effects. Paper waste is no longer incinerated but is now removed from site and recycled into office stationery which the Bank then purchases for its own use. The amount of paper waste leaving its premises in this manner does not appear to be recorded or monitored regularly. Being able to report quantified data such as this would be beneficial to the organisation in order to demonstrate its commitments and actions to its various stakeholders. There is no monitoring of energy use or emissions from Bank vehicles.

The branch expansion strategy is an area where Commercial Bank could minimise some of its direct environmental impact. Whilst most new branches are placed in leased premises, the Bank directly owns 32 and at least one new building is planned on an annual basis. Whilst quality aspects of both new buildings and retrofits are considered there are currently no environmental standards built into the project design stage (i.e. lighting, energy source, materials choice). All the Bank’s buildings are now fitted with energy saving bulbs. The most recent new building incorporated disabled access which is now the Bank’s minimum standard for projects.

Commercial Bank’s credit policy includes commitment to not entertaining the financing of illegal or unethical activities and avoiding situations where there is a threat to the environment. As a minimum requirement, where required by law, projects that need an environmental licence are only granted credit once the licence is in place. Accordingly, Lending Officers obtain clearance from Central Environmental Authority (a local statutory body) whenever they feel that a particular lending proposal has an adverse impact on the environment. Where the impact of the lending proposal on the environment is severe, the Lending Officers go to the extent of seeking an independent opinion from an expert in the particular field. This element of project lending is supported by a number of checklists within the department covering approval criteria and all loan evaluation forms contain a standard set of questions on environmental issues covering pollution controls and management responsibilities. Commercial



Bank conducts some directed lending towards environmental initiatives such as the 'e-Friends' Loan Scheme funded by the Japan Bank for International Cooperation.

Whilst international best practice considerations such as the Equator Principles and Principles for Responsible Investment are geared towards financial institutions of a larger and more international scale than Commercial Bank, the Bank did sign up to the UN Global Compact in 2002. Awareness of the UN Global Compact throughout the organisation has been raised through internal publications. However, interviews within the organisation indicated that attentiveness to the UN Global Compact and its requirements may not yet be fully embedded within the organisation. Some evidence of this is the fact that Commercial Bank is currently listed by the UN as being behind on its Communication on Progress and is at threat of being delisted from the participant list. Also the Bank disclosure on the UN Global Compact was not evident in the external publications.

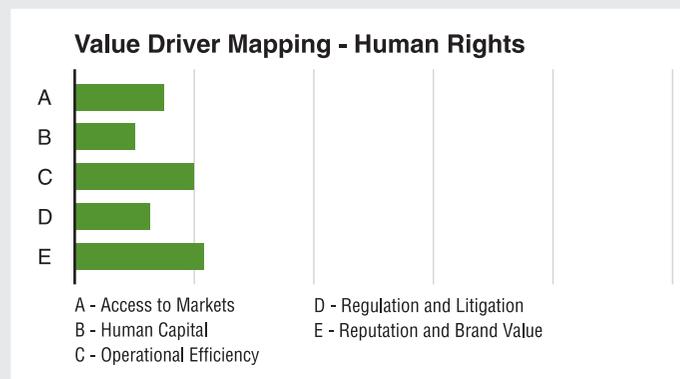
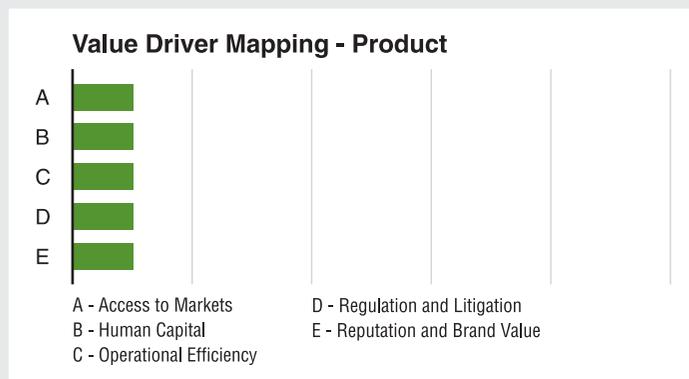
**Outline of risk**

Product: No discernible impact, no physical products. Issues of mis-selling etc. addressed in Market-place Human Rights: Retail banks rarely infringe on human rights. Access to banking services is not a core human right. Risk slightly increased in corporate banking operations although the nature and scale of Commercial Bank's activities mean limited impacts.

**Evaluation of management response**

These impacts are not a major concern to Commercial Bank. As discussed above, the Bank has previously signed up to the UN Global Compact but cannot demonstrate how considerations such as upholding human rights are being proactively managed beyond raising awareness amongst its employees.

**Social Impacts**



# ADDING VALUE AT MULTIPLE LEVELS

## Sustainability

Bank is a model corporate citizen. Its Mission is to “Redefine convenience in Financial Services”. It attempts to provide the “fruits” of its existence to all of its stakeholders around it, now and into the indefinite future. These “fruits” take various forms depending on the type of the stakeholder – creation of value and a decent dividend to the shareholders, a rate of interest that is commensurate with the risk of a private financial institution to the depositors and other debt capital holders, credit and related facilities at competitive rates of interest to the industry, content and rewarding employment to staff, tax revenue to the Government, a stable and sound financial institution as far as the regulators are concerned and above all, convenience and peace of mind to all of them.

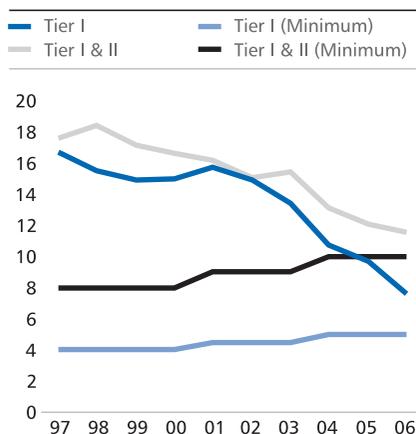
This section elaborates the “value” that the Bank has created and delivered to various stakeholders and the society at large.

Being the largest private sector bank in the country and as a result, being systemically important to the smooth functioning of the economy, the Bank conducts its activities adhering to principles of good corporate governance as detailed in the section on Enterprise Governance on page 64 of this Report. It conducts its business and operations in a highly transparent manner without prejudice to any person, group of people or segment of the society. The Bank’s policy has been to deliver optimum value in a manner that is consistent with the highest levels of fairness and transparency. It has not been a case of building financial value and enhancing the bottom line at any cost, but rather

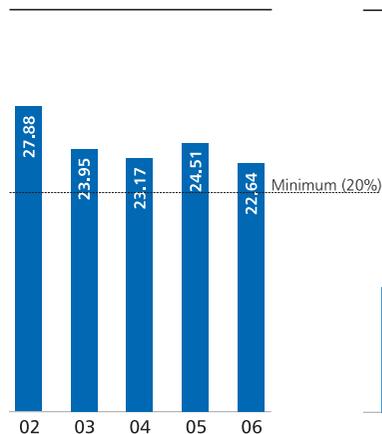
participating in a process of creating value through fair and ethical means. Building sustainable value for all stakeholders is one of the Bank’s important corporate goals.

Fitch Ratings Lanka Ltd. upheld the AA + (lka) national rating assigned to the Bank. Bank received an unqualified audit opinion on the financial statements from the statutory auditors for the year ended December 31, 2006. Bank continued to receive several awards and accolades during the year in appreciation of its efforts in maintaining sustainable performance and conducting business with transparency and full and fair disclosure. Bank has one of the lowest levels of non-performing assets among the banks in the country. As at December 31, 2006, the Bank recorded the Highest Market Capitalisation among all the financial institutions in the country.

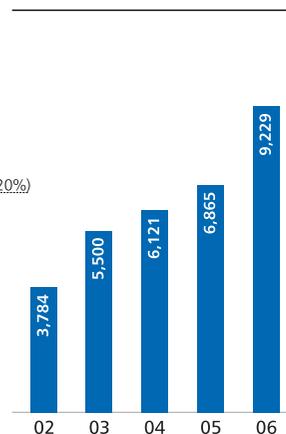
Capital Adequacy Ratio (%)



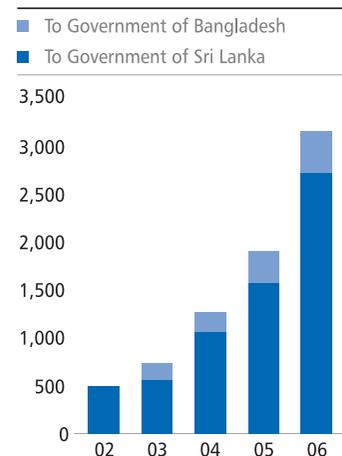
Liquid Assets Ratio (%)



Free Capital (Rs. Mn.)



Revenue to Governments (Rs. Mn.)



Bank's multiple delivery points consisting of 150 branches and service points and 269 ATMs which were available over 99% of the time, along with the concepts such as Supermarket Banking, Saturday Banking, 365-Day Banking, mobile ATMs etc. provide maximum convenience to various stakeholders in fulfilling most of their financial services related requirements.

Being conscious of the risks of overdependence on one economy, the Bank took several initiatives such as lending to Maldivian customers on off-shore basis, commencing banking operations in Bangladesh, getting into the money remittance business in several countries etc. to gradually reduce its dependence on the Sri Lankan economy. These initiatives have paid off as evident from the Bangladesh operations contributing Rs. 385.387 million to the profit after tax of the Bank in 2006. Our Sri Lankan operations provide IT support and training facilities to Bangladesh operations.

Bank is a major tax payer to the Government of Sri Lanka. During the year 2006, it paid over Rs. 2.000 billion in direct taxes comprising of Income Tax, Financial VAT, Social Responsibility Levy and Debits Tax. Further, the Bank collected and remitted several more billions in indirect taxes to the Revenue Authorities during the year.

### Managing Risks

In terms of a consultancy services agreement signed up with the Deutsche Bank, Asia Pacific Head Office, Singapore, the Bank will shortly commence upgrading its Risk Management infrastructure to international best practices. An Integrated Risk Management Department is being set up which will address all types of risks centrally: Credit, Market, Asset & Liability Management and Operations, when it is fully operational.

The Assets and Liabilities Committee and the Credit Committee meet regularly to review the market and credit related factors and recommend and implement suitable measures to counter associated risks.

Appropriate internal control measures and contingency plans are in place to address operational risks. The Board undertakes a bi-annual review of the Risk Management System. Detailed risk management measures in place are given in the article on Risk Management on page 76 of this Report.

### Payment of Dividends

The dividend policy of the Bank has always been to pay a decent dividend to its shareholders while ploughing back sufficient profits to fund growth and capital adequacy requirements. As a result of this prudent dividend policy, the Bank has been able to build up its shareholders' funds base to satisfactory levels. In fact, the

Commercial Bank has one of the highest levels of free capital among the banks in the country today.

Considering the performance of the Bank for the year, the Board has recommended a dividend of 50% for the year (of which 15% was paid in November 2006) compared to the 45% paid for 2005.

### Ensuring Resources Efficiency

Deposits, Borrowings and Shareholders' Funds represented the three biggest resources of funds for the Bank, accounting for 70.38%, 8.46% and 7.07% respectively of the total liabilities and shareholders' funds as at December 31, 2006. Mobilising deposits from stable and low cost sources and the prudent investment of funds are imperative for improving the profitability of the Bank. In addition, the Bank continued to mobilise funds from non-deposit sources such as Debentures, Syndicated Borrowings etc. to supplement deposit mobilisation efforts.

Through careful planning, a prudent dividend policy and controlling capital expenditure and investments, the Bank ensured that the Shareholders' Funds, the Free Capital and the Single Borrower Limit continued to grow. Total Shareholders' Funds, Free Capital and the Single Borrower Limit were Rs. 15,842.841 million, Rs. 9,228.971 million and Rs. 4,436.551 million respectively as at December 31, 2006.

**Maintaining Capital Adequacy**

Capital Adequacy symbolises the financial strength and stability of a bank. It limits the extent up to which banks can healthily expand their business in terms of risk weighted assets.

In the process of expansion, banks acquire property, plant & equipment, open branches, mobilise deposits, provide loans and invest in other assets. All these lead to constant changes in their risk profiles. Regulatory capital requirements are therefore necessary to prevent banks from expanding beyond their ability to manage (over trading), to improve the quality of banks' assets, to control the ability of the banks to leverage their growth and to lead to higher earnings on assets, ensuring stability

and soundness of a bank. The Bank attempts to ensure that capital keeps pace with its business expansion.

The Capital Adequacy Computation of the Group as at December 31, 2006 is given on page 49.

**Maintaining Liquidity**

The Bank maintains a consistent liquidity policy in its operations and carries a positive mismatch in the interest earning assets and interest bearing liabilities in the 1 to 30 day category. The Bank functioned at optimum liquidity levels throughout the year. If and when the liquidity falls below the internally set limits which is above the mandatory limits, the Bank took effective and prompt actions to fund the shortfall in liquidity by way of borrowings. The Liquid Assets Ratio stood at 22.64% in December 2006.

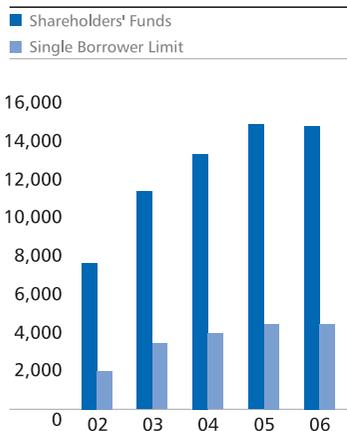
The Assets and Liabilities Committee (ALCO) of the Bank continuously monitors the liquidity level with a view to maintaining a satisfactory trade-off between liquidity and profitability.

**Content and Rewarding Employment to Staff**

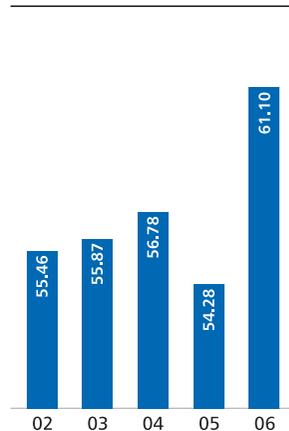
The Bank's total staff strength as at end 2006 was 3,415. Of them, 388 are new recruits during the year.

141 employees retired or resigned during the year. Various measures that the Bank has taken in this regard over the year are detailed in page 58. The Bank believes that these measures have immensely helped to improve people productivity, work-life balance and knowledge and skills of the employees, in taking the Bank to even higher levels as envisaged by the Vision and strategic direction.

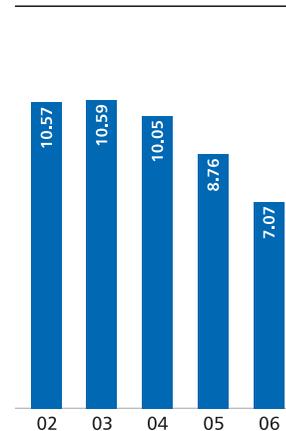
**Shareholders' Funds/ Single Borrower Limit (Rs. Mn.)**



**Cost/Income Ratio (%)**



**Shareholders' Funds/ Total Liabilities and Shareholders' Funds (%)**



## Capital Adequacy Computation - Group

### Computation of Risk-Weighted Assets

Assets	Balance		Risk-Weight Factor (%)	Risk-Weighted Balance	
	2006	2005		2006	2005
	Rs. '000	Rs. '000		Rs. '000	Rs. '000
Cash, Statutory Deposit with Central Banks					
Treasury Bills, Government and other Securities	38,371,428	22,497,900	-	-	-
Facilities secured by Cash and guaranteed by					
Central Bank of Sri Lanka	17,965,957	13,198,084	-	-	-
Facilities guaranteed by Local/					
Foreign Commercial and Development Banks	1,003,444	-	20	200,689	-
Guaranteed by OECD Incorporated Banks	1,417	-	20	283	-
Loans guaranteed by SLECIC	200	8,000	50	100	4,000
Loans secured by Primary Mortgages					
over Residential Property	-	8,226,039	50	-	4,113,020
Loans secured by Primary Mortgages					
over Residential Property	11,864,148	-	55	6,525,281	-
Other Loans and Advances	-	97,617,906	100	-	97,617,906
Other Loans and Advances	122,316,000	-	110	134,547,600	-
Credit Equivalent of Off-Balance Sheet Items	12,044,944	11,005,297	100	12,044,944	11,005,297
Due from Banks Abroad	8,506,479	15,723,987	20	1,701,296	3,144,797
Due from Local Banks including					
Development Financial Institutions	1,949,872	376,010	20	389,974	75,202
Due from Off-shore Banking Centre	-	-	10	-	-
Cash Items in the process of collection	134,139	122,317	20	26,828	24,463
Investments excluding Investments in					
Financial Associates	1,404,455	2,204,710	100	1,404,455	2,204,710
Property, Plant & Equipment and Intangible Assets	3,600,295	3,516,183	100	3,600,295	3,516,183
Other Assets	4,480,652	3,991,381	100	4,480,652	3,991,381
<b>TOTAL</b>	<b>223,643,430</b>	<b>178,487,814</b>		<b>164,922,397</b>	<b>125,696,959</b>

### Credit Equivalent of Off-Balance Sheet Items

Instruments	Balance		Credit Conversion Factor (%)	Risk-Weighted Balance	
	2006	2005		2006	2005
	Rs. '000	Rs. '000		Rs. '000	Rs. '000
General Guarantees of Indebtedness					
(Credit Guarantees and Advance					
Payment Guarantees)	9,406,754	6,279,508	100	9,406,754	6,279,508
Performance Bonds, Bid Bonds					
and Warranties	3,960,924	3,419,905	50	1,980,462	1,709,953
Shipping Guarantees	1,314,119	1,117,648	20	262,824	223,530
Documentary Letters of Credit	9,591,240	9,373,307	20	1,918,248	1,874,661
Usance Bills	4,937,977	4,517,958	20	987,595	903,592
Bills for Collection	5,016,267	4,346,833	-	-	-
Foreign Exchange and Interest Rate					
related Contracts:					
Customers	31,922	19,718	50	15,961	9,859
Banks	52,011	20,969	20	10,402	4,194
<b>Total</b>	<b>34,311,214</b>	<b>29,095,846</b>		<b>14,582,246 *</b>	<b>11,005,297</b>

\* The credit equivalent of these off-balance sheet items has been risk weighted based on rates applicable for the underlying securities.

## Economic Impact Report

### Capital Adequacy Computation - Group (Contd.)

#### Computation of Capital

	2006		2005	
	Rs. '000	Rs.'000	Rs. '000	Rs. '000
<b>TIER I : Core Capital</b>				
Paid-up Ordinary Shares	1,428,186		1,420,809	
Share Premium	1,728,793		1,679,604	
Statutory Reserve Fund	1,429,319		1,421,819	
Published Retained Profits	68,165		83,869	
General and other Reserves	8,394,453		7,550,789	
Minority Interest	11,023		13,285	
Less: Goodwill	-		-	
Total Tier I Capital	13,059,939		12,170,175	
Less: Loans Granted under ESOP Scheme	(343,251)	12,716,688	-	12,170,175
<b>TIER II : Supplementary Capital</b>				
Revaluation Reserve (as approved by the Central Bank of Sri Lanka)	651,037		651,037	
General Provisions	238,622		85,411	
Approved Subordinated Term Debt	5,746,994		3,455,646	
Total Tier II Capital		6,636,653		4,192,094
Total Capital		19,353,341		16,362,269
<b>Deductions</b>				
Investments in Banks and Financial Associates		33,754		1,176,084
Capital Base		19,319,587		15,186,185

#### Computation of Ratios

	2006		2005	
	Rs. '000		Rs. '000	
<b>Total Risk-Weighted Assets (RWA)</b>				
Total Risk-Weighted Assets for Credit Risk	164,922,397		125,696,959	
Total Risk-Weighted Assets for Market Risk	1,894,190		-	
Sub Total	166,816,587		125,696,959	
<b>Minimum Capital Charge</b>				
Capital Charge for Credit Risk	16,492,240		12,569,696	
Capital Charge for Market Risk	189,419		-	
Sub Total	16,681,659		12,569,696	
<b>Total Capital available to meet the Capital charge for Credit Risk</b>				
Total Tier - I Capital	12,716,688		12,170,175	
Tier - II Capital (after deducting investments in Banks and Financial Associates)	6,602,899		3,016,010	
Sub Total	19,319,587		15,186,185	
<b>Core Capital Ratio (Minimum Requirement 5%)</b>				
Total Tier - I Capital	12,716,688		12,170,175	
Total Risk Weighted Assets	166,816,587		125,696,959	
	7.62%		9.68%	
<b>Total Capital Ratio (Minimum Requirement 10%)</b>				
Total Capital	19,319,587		15,186,185	
Total Risk Weighted Assets	166,816,587		125,696,959	
	11.58%		12.08%	

#### Risk-Weighted Assets

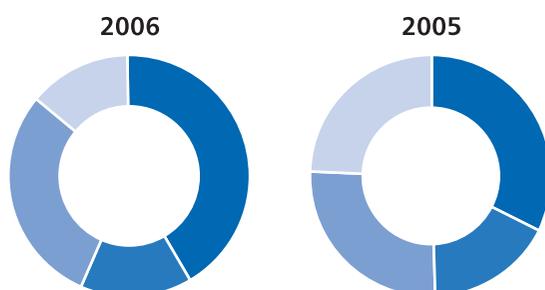
- Loans and Advances are net of specific provisions and interest in suspense.
- Total assets do not tally with that of the Balance Sheet mainly due to differences in treatment on securities sold under repurchase agreements and investments in capital of other banks/financial institutions in the capital adequacy computation.

## Value Addition

	2006		2005	
	Rs. '000	%	Rs. '000	%
<b>Value Added</b>				
Income from Banking Services	23,234,534		15,578,410	
Cost of Services	(13,232,604)		(8,381,402)	
Value Added by Banking Services	10,001,930		7,197,008	
Non-Banking Income	1,234,936		521,235	
Loan Losses and Provisions	(655,070)		(414,864)	
	<b>10,581,796</b>		<b>7,303,379</b>	
<b>Distribution of Value Added</b>				
<b>To Employees</b>				
Salaries and other Benefits	4,373,556	41.32	2,364,148	32.37
<b>To Providers of Capital</b>				
Dividends to Shareholders	911,413		869,716	
Interest to Debentureholders	641,540		371,049	
	<b>1,552,953</b>	<b>14.68</b>	<b>1,240,765</b>	<b>16.99</b>
<b>To Governments</b>				
Income Tax	2,191,641		1,301,974	
Financial Value Added Tax	970,958		622,936	
Debits Tax	6,418		4,119	
	<b>3,169,017</b>	<b>29.95</b>	<b>1,929,029</b>	<b>26.41</b>
<b>To Expansion and Growth</b>				
Retained Profit	1,101,215		1,494,524	
Depreciation	375,779		299,167	
Deferred Taxation	9,276		(24,254)	
	<b>1,486,270</b>	<b>14.05</b>	<b>1,769,437</b>	<b>24.23</b>
	<b>10,581,796</b>	<b>100.00</b>	<b>7,303,379</b>	<b>100.00</b>

## Distribution of Value Added

	2006	2005
■ To Employees	41%	32%
■ To Providers of Capital	15%	17%
■ To Government	30%	26%
■ To Expansion and Growth	14%	25%



## Economic Impact Report

### Economic Value Added

Economic Value Added (EVA) is a measure of profitability which takes into consideration the cost of total invested equity.

	2006	2005	2004	2003	2002
	Rs. '000	Rs. '000	Rs. '000	Rs. '000	Rs. '000
<b>Invested Equity</b>					
Shareholders' Funds	14,842,841	13,861,828	12,004,962	9,777,402	6,848,102
Add: Cumulative Loan Loss Provision	2,536,465	2,192,293	2,053,828	1,668,752	1,099,155
	17,379,306	16,054,121	14,058,790	11,446,154	7,947,257
<b>Earnings</b>					
Profit after Taxation and Dividends					
on Preference Shares	1,815,210	2,133,888	1,454,362	1,287,820	1,086,162
Add: Loan Losses and Provisions	655,070	414,864	699,200	623,207	401,972
Less: Loan Losses Written Off	(7,698)	(5,011)	(9,138)	(81,588)	(19,550)
	2,462,582	2,543,741	2,144,424	1,829,439	1,468,584
Cost of Equity Based on the 12 months					
Weighted Average Treasury Bill Rate plus					
2% for the Risk Premium	12.91%	10.87%	9.65%	10.00%	12.00%
Cost of Average Equity	2,158,128	1,636,637	1,230,614	969,671	873,076
<b>Economic Value Added</b>	<b>304,454</b>	907,104	913,810	859,768	595,508

At Commercial Bank, we are deeply conscious of delivering value to all our stakeholders consistently.

We still remain one of the very few companies in Sri Lanka that has embraced EVA as a measure of performance.

In EVA terms, we have created Rs. 304.454 million during the year 2006 and over Rs. 3.500 billion over the past 5 years.

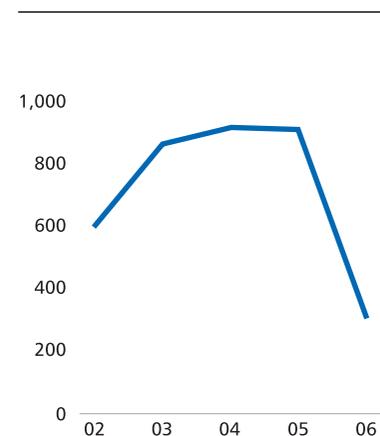
### Maturity Analysis

The Assets and Liabilities Committee of the Bank closely monitors the maturities of assets and liabilities of the Bank.

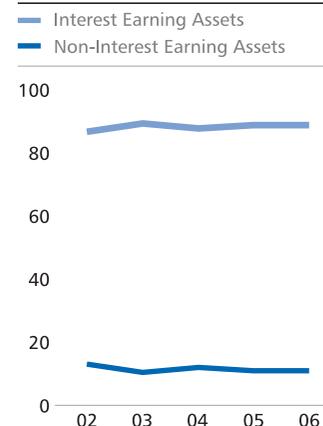
A summary of the maturity pattern of the respective assets and liabilities of the Bank as at December 31, is as follows:

Item	Maturity Period					Total 2006	Total 2005
	Up to 3 months	3 - 12 months	1 - 3 years	3 - 5 years	Over 5 years		
	Rs. '000						
Interest Earning Assets	95,017,606	26,630,624	52,575,623	12,295,350	13,224,353	199,743,556	160,018,609
Non-Interest Earning Assets	17,528,175	2,233,102	81,974	53,234	4,334,212	24,230,697	20,058,854
<b>Total Assets</b>	112,545,781	28,863,726	52,657,597	12,348,584	17,558,565	223,974,253	180,077,463
Interest Bearing Liabilities	121,859,018	40,387,659	6,456,065	3,310,117	6,695,017	178,707,876	144,593,017
Non-Interest Bearing Liabilities	27,843,770	999,231	1,000,000	580,535	14,842,841	45,266,377	35,484,446
<b>Total Liabilities</b>	149,702,788	41,386,890	7,456,065	3,890,652	21,537,858	223,974,253	180,077,463
Maturity Gap	(37,157,007)	(12,523,164)	45,201,532	8,457,932	(3,979,293)		
Cumulative Gap	(37,157,007)	(49,680,171)	(4,478,639)	3,979,293	-		

### Economic Value Added (Rs. Mn.)



### Asset Mix (%)



# EXPLODING... AND EXPLORING OUR GENIUS

## Beyond Financial Performance

The Bank has led the way with corporate reporting in this country. We have set new standards for clarity and transparency and sought to project as complete a picture of our corporate operations as possible. This is our responsibility as a publicly listed company and as the leading private financial institution in the country. It is an obligation of any who aspires to be a model corporate citizen.

This year too, with the goal of enhancing transparency and exposing every aspect of the Company's performance, we have sought to report on aspects of the Company's performance that go 'beyond the financials'. In this section we profile and document the 'invisibles' that have driven performance in the past year.

The Bank's Knowledge Capital consists of those soft factors that create value for all stakeholders. Our Knowledge Capital – consisting of our Human Capital and our Structural Capital – has been a key driver of our corporate success over the years.

The Bank's **Human Capital** – consisting of staff skills, capacities, talents, attitudes, business routines, work ethics, mindsets, emotions and imaginations – have achieved new benchmarks in performance over the previous year.

The Bank's Human Capital has helped create a rich base of Structural Capital which has been equally vital in the Bank's overall performance. The Bank's **Structural Capital** – consisting of its brands, product portfolios, databases, software, work procedures, experience, know-how, organisational culture, information management systems and other work systems - has played an equally important role in our success. Seeking the perfect blend between these two types of capital ensures optimal performance and builds value for all stakeholders.

## Knowledge Smart

Our process of managing knowledge capital at the Bank has focused on striking the perfect mix between human and structural capital. While human capital 'leaves' the organisation everyday and sometimes can leave the organisation

permanently, structural capital accrues to the organisation in a more sustainable way. Striking this fine balance is a corporate art.

Effective knowledge management strategies also require generating capacities to adapt. Adapting to social and political change, lifestyle change, weather change, market change and just natural processes of change is a sine qua non for staying at the top. As a top performer the Bank must be capable of performing in good times and in bad. Merely because the going gets tough, the organisation should not get rough.

Our knowledge management strategy at the Bank is guided by five key values: integrity, effectiveness, passion, innovation and leadership. In redefining financial convenience we have integrated all these values into every aspect of our corporate governance and performance.

In today's world, knowledge is the primary catalyst of wealth creation: organisational, social and employee. This section is a tribute to this knowledge which has continued to create new wealth.



KNOWLEDGE BASED CAPITAL

BUSINESS PROCESSES

RANGE OF SERVICES

MISSION STATEMENT
KNOWLEDGE GOALS
STRATEGY 2007-2011

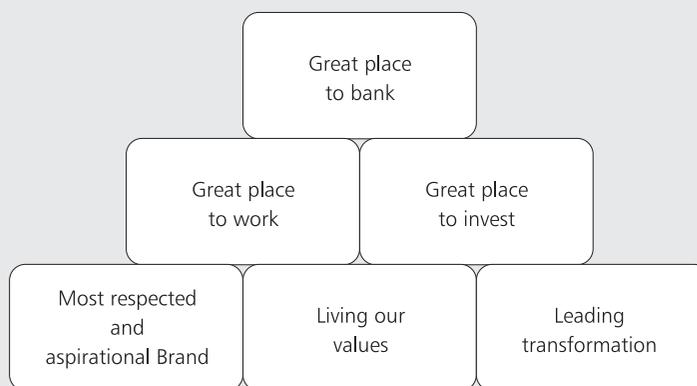
HUMAN CAPITAL
STRUCTURAL CAPITAL

Deposits Management
Loans Management
Asset & Liability Management
Channel Development
Operations Management
Risk Management
Data Management
Capacity Building
Human Resource Management
Corporate Planning & Budgeting
Financial Management
Marketing Management

Accepting Deposits
Corporate and Retail Credit
Project Financing
Leasing
Personal Loans
Trade Financing
Travel Related Services
Issuing of Local and International Credit Cards
Tele Banking Facilities
Internet Banking
Bullion Trading
Export & Domestic Factoring
Dealing in Government Securities
Inward and Outward Remittance Services
ATM Services
Advisory Services
Securitisations
IPO Management
Structuring Corporate Debts
Sponsor of the Colombo Stock Exchange
Bancassurance
Salary Remittance Package
Priority Banking
Holiday Banking
Reloading Mobile Phones
Foreign Currency Swaps
Interest Rate Swaps
Foreign Exchange Dealings

**Vision** to be the PREFERRED financial services organization in Sri Lanka, having an international presence by the year 2011

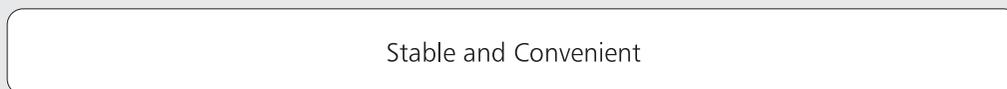
Our Aspirations



What makes us unique and guides our long-term strategy



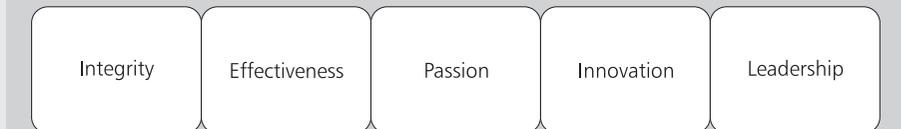
Our brand expression



Strategic focus areas



Our values



### Great Aspirations

As a financial services organisation we aspire to be nothing but the best. We want to be a great place to bank at, a great place to work in and a great place to invest in. We want to be the most respected brand that engages in entrepreneurship according to our strong corporate values. We also want to be a trail-blazer, a pioneer and lead agent in social and corporate transformation creating new opportunities for all people and adding value wherever we are.

### Human Capital

#### Unleashing Hidden Energy

While inspiring our human resource base, we have endeavoured at all times to ensure that they enjoy the optimum benefits and rewards for their imagination and labour. Like all relationships, we have nurtured a win-win scenario for both employer and employee. The full potential of a human resource pool can only thrive in an environment in which they are comfortable and inspired. Tension and discomfort are not catalysts of productivity and innovation. Our aspiration is to make the Bank a great place to work in.

In March 2006 we signed a watershed agreement with the Ceylon Bank Employees' Union (CBEU). The new collective agreement recognised the changing environment in which our employees had to operate and sought to ensure that the organisation provides the optimum benefits proportionate to the Company's performance and standing.

The new Collective Agreement covers Junior Executive Assistants and Allied Grades, Banking Assistants and Allied Grades and Minor Staff for a period of three years.

The new agreement was signed the moment the previous agreement came to an end and this itself was a significant achievement. Seldom has the financial services industry witnessed such smooth transition from one agreement to another and we set a milestone in industrial relations in this country.

The Collective Agreement was supplemented by an MOU with regard to the allowances and other benefits pertaining to the Junior Executive Officers of the Bank.

The Management dialogues regularly with the employee organisations and tries to nip any conflict and tension at an early stage. Our dialogue also extends to performance issues and we are joint partners in raising the Bank's level of performance to an even higher level.

Our sporting events, competitions and other events have succeeded in building a strong team spirit among all categories of staff and provided opportunities for families to bond. The Bank Newsletter "Compulse" is a vital tool of communication, from management to employees and vice versa.

### Rewarding Performance

In 2006 the Bank introduced a new Performance Rewards Plan for its employees based on which performance for 2007 onwards will be rewarded. Our new plan seeks to motivate employees to achieve specified business results, attract and retain the high quality talent for sustained business growth, promote a stronger team based performance culture and reinforce prioritised business strategies. The new plan was devised in partnership with Hewitt Outsourcing Services (India) Ltd.

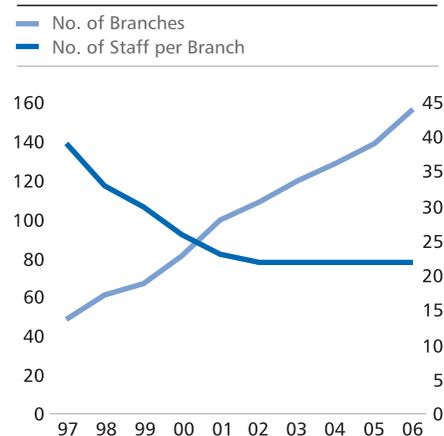
New organisational level thresholds were introduced in order to 'de-risk' business performance and the new payment scheme is linked very closely to the achievement of a minimum level of performance. Employees at senior levels in an organisation have a higher capacity to impact on the Bank's overall results, and this variable in employee capacity was also taken into account in designing the new scheme.

**Commercial Bank continues to maintain the leading position in terms of people productivity. This is confirmed by the following indicators:**

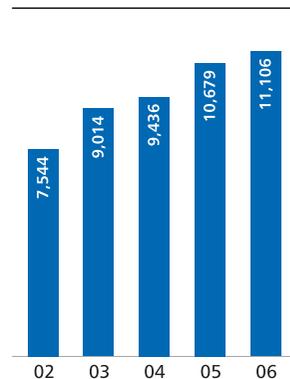
	2006	2005	2004	2003	2002
Staff per branch	<b>22</b>	22	22	22	22
Income per employee (Rs.'000)	<b>7,165</b>	5,082	4,293	3,799	3,486
Profit before tax per employee (Rs.'000)	<b>1,234</b>	1,150	875	739	636
Assets per employee (Rs.'000)	<b>65,585</b>	56,843	48,367	41,646	30,576

Year	No. of Employees	Total Value of Human Resource Rs. '000	Value of Human Resource per Employee Rs. '000
<b>2006</b>	<b>3,415</b>	<b>37,925,315</b>	<b>11,106</b>
2005	3,168	33,830,883	10,679
2004	2,863	27,014,491	9,436
2003	2,648	23,867,760	9,014
2002	2,399	18,098,299	7,544

**No. of Branches & No. of Staff per Branch**



**Value of Human Resource per Employee (Rs.'000)**



**Human Resource Accounting**

The Lev & Schwartz model has been used to compute the value of the Bank's human resource as at December 31, 2006.

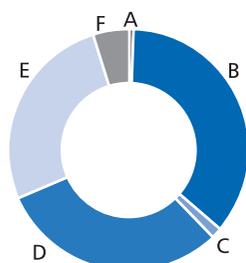
The Human Resource Valuation is based on the following assumptions:

- o All the existing employees will continue in employment up to retirement.
- o Employee remuneration includes all direct and indirect benefits earned by them.
- o Annual increment is granted at 10%-14% p.a. on average.
- o Total future remuneration of all the employees for each year is discounted to the present value at 12.91%, the 12 months weighted average treasury bill rate plus 2% for the risk premium.

# Knowledge Management Report

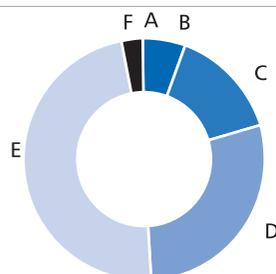
## Staff Strength - 2006

A CM - 1%	D JEA - 31%
B EO - 35%	E BT - 27%
C EA - 1%	F OA - 5%



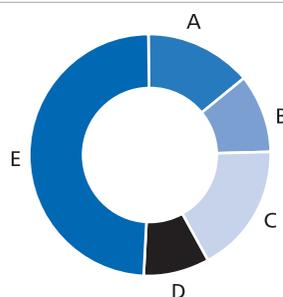
## Age Analysis - 2006

A Above 60 - 0%	D 31 - 40 - 28%
B 51 - 60 - 6%	E 21 - 30 - 48%
C 41 - 50 - 15%	F 20 & Above - 3%



## Service Analysis - 2006

A Above 20 - 15%	D 6 - 10 - 9%
B 16 - 20 - 10%	E 25 & Above - 49%
C 11 - 15 - 17%	



## Staff Strength

As at December 31,	2006	2005	2004	2003	2002
Corporate Management (CM)	17	15	15	14	14
Executive Officers* (EO)	1,225	1,093	1,001	918	787
Executive Assistants and Allied (EA)	46	66	53	62	23
Junior Executive Assistants and Allied (JEA)	1,053	1,008	942	798	813
Banking Trainees (BT)	911	819	677	672	574
Office Assistants and Others (OA)	163	167	175	184	188
<b>Total</b>	<b>3,415</b>	<b>3,168</b>	<b>2,863</b>	<b>2,648</b>	<b>2,399</b>

## Age Analysis of the Staff as at December 31,

Age Group (Years)	Corporate Mgt.	Executive Officers	Executive Assistants & Allied	Jr. Exe. Assistants & Allied	Banking Trainees	Office Asst. & Others	2006 Total	2005 Total
Above 60	-	2	-	-	-	-	2	2
51 - 60	12	124	2	24	-	31	193	144
41 - 50	4	278	18	138	-	82	520	507
31 - 40	1	597	14	293	1	48	954	980
21 - 30	-	224	12	597	815	2	1,650	1,453
20 & below	-	-	-	1	95	-	96	82
<b>Total</b>	<b>17</b>	<b>1,225</b>	<b>46</b>	<b>1,053</b>	<b>911</b>	<b>163</b>	<b>3,415</b>	<b>3,168</b>

Average age of the employees as at December 31, 2006 was 34.2 years (2005 - 32.3 years).

## Service Analysis of the Staff as at December 31,

Service Group (Years)	Corporate Mgt.	Executive Officers	Executive Assistants & Allied	Jr. Exe. Assistants & Allied	Banking Trainees	Office Asst. & Others	2006 Total	2005 Total
Above 20	12	315	11	78	-	82	498	482
16 - 20	-	211	9	98	-	30	348	271
11 - 15	1	342	4	186	-	49	582	645
6 - 10	1	171	3	122	-	2	299	373
5 & below	3	186	19	569	911	-	1,688	1,397
<b>Total</b>	<b>17</b>	<b>1,225</b>	<b>46</b>	<b>1,053</b>	<b>911</b>	<b>163</b>	<b>3,415</b>	<b>3,168</b>

Average service of the employees as at December 31, 2006 was 10.0 years (2005 - 10.0 years).

The service of the employees absorbed from Eastern Bank Ltd. and Mercantile Bank Ltd. is also included.

\* Inclusive of Management Trainees, Confidential Secretaries and Employees on Contract.

## Staff Recruitment

	2006	2005	2004
Banking Trainees	378	352	292
Management Trainees	4	5	13
Other	6	14	10
Total	388	371	315

## Response Rate for Vacancy Advertisements - 2006

Banking Trainees	15,000 (Approximately)
Management Trainees	1,000 (Approximately)
No. of Unsolicited Applications	3,000 (Approximately)

## Staff Retention

	2006	2005	2004
Staff Retention - Sri Lanka (%)	96.13	97.37	97.26
Staff Retention - Bangladesh (%)	91.53	94.44	85.95
Total (%)	93.83	95.91	91.61

## Training & Development

	2006	2005	2004
Training & Development Cost (Rs. Mn)	35.794	32.504	30.081
Training Development cost per Employee (Rs.)	10,481	10,260	10,507
T&D Cost as a % of Personnel Cost	1.40	1.53	1.67

## Staff Welfare

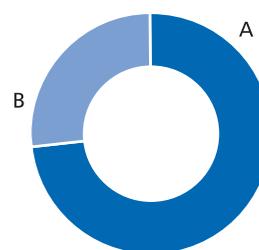
	2006	2005	2004
Staff Welfare Cost (Rs. Mn.)	59.287	42.401	33.316
Staff Welfare Cost per Employee (Rs.)	17,361	13,384	11,637
Staff Welfare Cost as a % of Personnel Cost	2.31	1.99	1.84

## Training Programmes

Year	In-house			Other Local Institutions			Overseas			Total		
	No. of Programmes	No. of Participants	Training man hours	No. of Programmes	No. of Participants	Training man hours	No. of Programmes	No. of Participants	Training man hours	No. of Programmes	No. of Participants	Training man hours
2006	223	6,290	91,974	144	1,180	22,099	52	103	2,806	419	7,573	116,879
2005	214	6,566	89,499	119	457	19,381	35	58	1,960	368	7,081	110,840
2004	206	6,571	85,255	133	391	21,175	40	72	2,185	379	7,034	108,615

## Gender Distribution - 2006

A Male - 73%    B Female - 27%



## Gender Distribution

As at December 31, 2006	Male	Female
Corporate Management (CM)	16	1
Executive Officers* (EO)	894	331
Executive Assistants and Allied (EA)	39	7
Junior Executive Assistants and Allied (JEA)	641	412
Banking Trainees (BT)	746	165
Office Assistants and Others (OA)	163	0
Total	2,499	916

A new Performance Appraisal System was introduced as well. The new system moves away from the previous Management by Objectives (MBO) approach to a 'Key Performance Indicators' (KPI) approach. The new system is based on four pillars: Goal setting and establishing accountabilities; Review and measurement; Performance feedback and coaching; and Alignment to HR systems.

### **Re-Defining Terminal Benefits**

The previous pension plan of the Bank, based on a 'Defined Benefit Plan' (DBP) model was restructured and brought in line with current global practices. The previous plan exposed the Bank to huge funding deficiencies, particularly at times when interest rates were not keeping pace with salary increases.

Globally, DBPs are on the decline and financial institutions are increasingly adopting pension plans based on a Defined Contribution Plan model. In addition to inherent issues such as pooled funding, vesting conditions and vulnerability of assumptions associated with DBPs, they provide little transparency, simplicity and ease of understanding.

This compelled the Bank to devise an alternative scheme which is both employer and employee friendly. In partnership with Hewitt Outsourcing Services (India) Ltd., the Bank introduced a new pension plan and a

vast majority of the staff subscribed to this new scheme. The new pension scheme will be managed by the members of the management and representatives of the worker organisations.

### **Replenishing and Polishing our Human Capital**

Two things are vital for a vibrant human capital: a constant replenishment of new people with new ideas and new energy and a polishing of existing skills through an exposure to new training and new knowledge.

We have managed to tailor our policies so that we do both of these smartly and efficiently. Competent and committed staff ensure excellent customer service standards. Accordingly, our recruitment and selection processes are constantly reviewed and improved. We introduced new criteria and selection methods to ensure that we attract the best. The Bank is also involved in the conducting of career programmes to help younger Sri Lankans select the right careers. Last year we used 'Assessment Centres' for the first time as a selection tool in addition to the regular written tests and the interview processes to select new Management Trainees.

Bank staff is constantly exposed to new skills, new technologies, new systems, new processes, new ideas and new knowledge. Our training programmes have a strong link with individual staff member career

aspirations and we try to ensure that both Bank and employees benefit from the programmes we constantly expose our staff to. Last year we conducted 116,879 man hours of training consisting of technical skills, personal effectiveness, services enhancement and IT skills.

Branches developed a comprehensive Service Quality Manual covering the service value chain. Customer service standards were established to sustain the consistency of service levels and this was further assessed by carrying out 'Mystery Audits' to ensure a higher level of accountability.

We ensure that we maintain a strong faculty of resource persons both internal and external for our in-house programmes. Our staff is also exposed to training both overseas and locally.

Our Bangladesh Operation trained its staff through in-house programmes, locally held external programmes and overseas programmes, most of which were in Sri Lanka.

The placement of staff as Business Promotions Officers in select locations called for specialised programmes of training. This focused on Marketing, Cross Selling, Negotiation Skills and Cross Cultural etiquette.

Last year we promoted 216 members to new positions. These promotions are a reflection of the Bank's growth

and the employees' growth. Inspiring and motivating employees is part of our promotional policy. The eligibility criteria for the position of Junior Executive Officer were changed taking into consideration the new job demands.

In addition to the recruitment of employees, the Bank continued the outsourcing of the non-core banking areas, a practice which commenced some years ago.

**Filling the 'Big Shoes'**

'Succession Planning' is now an important part of any Human Capital management strategy. The Bank has taken steps to integrate a systematic approach to 'succession' to ensure that key organisation gaps are easily filled and the exit of any one or more persons does not create transition problems. Succession gaps and future staffing gaps are quickly identified and processes soon put in place to respond to these needs. Two important values have shaped our response in this regard: minimum disruption and sustainability of operations.

Our Succession Plan is synchronised with the Bank's business strategy and the Bank's short- and long-term objectives. We have developed a 'Leadership Capability Model' which helps the Bank identify future leaders and successors.

A 'Capability Profile' of all potential successors has been developed and a 360 Degree Feedback/ Multi-Rater Feedback System was institutionalised with the assistance of Professor T. V. Rao, an Indian Human Resource guru.

This model known as the 'RSDQ Model' (Roles, Styles, Delegation and Qualities) employs a number of criteria and processes to flag leadership quality. Assessments from direct superiors, direct reports from subordinates and colleagues and an assessment from internal customers, are among the criteria used in this process. All potential successors were assessed by approximately over 300 assessors during the past year and the data that was generated is being collated in order to plan future organisational training needs. The information provides both quantitative and qualitative data.

**Innovation Capital**

An important aspect of our knowledge management strategy is sustainability. Being able to constantly think afresh and break new frontiers in ideas ensures that a company stays on top. This means reading customer minds and responding to their inner most needs. It also means not just reacting to market trends but being proactive and establishing new market trends. This section documents how we have leveraged our flair to build new levels of convenience for all our customers.

Innovation	Year of Launch
<b>Sri Lanka</b>	
Holiday Banking	1998
Supermarket Banking (Staple's Street)	1999
Banking facilities for differently-abled	2004
Mobile ATM	2005
Top Up facility	2005
Tiered Savings Account	2005
On-line Cheque Viewing facility	2006
<b>Bangladesh</b>	
Holiday Banking	2005

**Tracking cheque payments on line**

The Bank unveiled in 2006 an innovative cheque viewing facility for its customers. Bank's customers can now view images of cleared and paid cheques issued by them, online, from their own homes and offices by merely clicking an icon on 'ComBank Online,' the Bank's Internet Banking system. This facility is available to all our Internet Banking customers. The Bank is the first in this country to offer this facility to its customers.

We are in the process of developing software to enhance this facility by enabling customers to track cheques they deposit in their accounts. We hope to have this system up and running by the end of the year.

	2006	2005	2004
<b>Information Technology</b>			
Additions during the year - Computer Software (Rs. Mn)	<b>96.66</b>	44.10	55.89
Additions during the year - Computer Hardware (Rs. Mn)	<b>176.28</b>	302.61	128.99
Total IT Development Expenditure (Rs. Mn)	<b>272.94</b>	346.72	184.88
IT Expenditure (Rs.Mn)	<b>710.53</b>	692.35	494.55
IT Development Expenditure as a % of IT Expenditure	<b>38.41</b>	50.08	37.38
IT Expenditure as a % of Administration Expenditure	<b>9.29</b>	14.37	11.75
ATM Cards Issued	<b>254,993</b>	201,299	189,543
Credit Cards Issued	<b>19,752</b>	18,382	9,830
No. of ATMs	<b>269</b>	223	188
No. of ATM Transactions per day (Average)	<b>41,722</b>	32,448	25,055
Amount of Cash Disbursed through ATMs per day ( Average) (Rs.Mn)	<b>178.52</b>	127.93	93.45

### Public Relations

No. of Press Conferences *	<b>2</b>	2	2
No. of Press Releases	<b>44</b>	43	39

\* Annual Report Press Conference & Debenture Issue Press Conference

### Procurement

Calls for Tenders	<b>202</b>	210	244
No. of Active Suppliers (Average)	<b>177</b>	174	166

### Moving towards a Cashless World

Our new Visa Debit does away with the need to carry cash. Unlike the credit card, the transaction amount is debited immediately to the customer's account. The debit card can be used at more than 29 million locations worldwide, including 7,000 local merchants.

The Bank identified a growing market for debit cards especially with the imposition of stamp duty and other taxes on credit card transactions. The debit card ensures that customers do not pay any excess charges for their transactions and also helps them keep better control over their purchases without the burden of having to carry large amounts of cash.

### Topping Up with Texts

In 2005, the Bank pioneered yet another product, the COM-eLoad facility. This enabled Dialog KIT prepaid mobile customers to top up their phone balances through an SMS. We are working to offer this facility for post-paid customers as well for settling their bills. It will also be offered to both pre-paid as well as post-paid customers of other service providers shortly.

**Higher interest with simulated foreign currency accounts**

We will soon allow customers the option of opening 'simulated foreign currency trading accounts' that will offer the potential of earning higher interest. FX Link, a capital guaranteed structured deposit product, which the Bank designed in 2006, will be launched in the early part of 2007.

**'Power Savings' grows**

The rebranded Power Savings Account continues to offer customers a 100% bonus on interest if no withdrawals are made during a quarter. The bonus interest is reduced to 50% if only one withdrawal is made.

Our tiered saving account ComLeap has drawn an immense response. To make the product even more attractive, the Bank recently increased the interest rates, offering our customers an even better return on their deposits.

**Directing Lending towards sustainability**

The Bank continued to help industries through the E Friends - II Loan Scheme. The scheme can be used to purchase equipment that leads to a reduction of emission, improvement in safety at the workplace and reduction in the use of resources by existing equipment. Under this loan scheme the Bank also helps highly polluting industries to relocate to special estates that are equipped with special waste treatment plants.

**Instant money transfers across the globe**

'Instant money transfers' through the Internet was another product we launched in 2006. In partnership with "MoneyGram", the global funds transfer company, we pioneered a real time money transfer system that is fast, low cost and efficient.

This facility is available in over 104,000 locations in 170 countries. These funds can be collected on any day of the year through the Bank's holiday banking facility, which is now

available in most parts of the country. They can also be collected from supermarket counters which are open till 7.30 p.m. everyday. The full amount remitted is paid and the beneficiary incurs no charges.

**Multiple options to multiple customers**

The Bank is now present, not just through the Internet and phone banking, but physically, in 125 branches, 7 CSPs, 17 Supermarket outlets and a Counter at the Bandaranaike International Airport. Last year we opened our 150th delivery point and our 269th ATM.

The Bank opened two new branches in Bangladesh last year. These new branches in Syhlet and Uttara, will enhance our presence and brand in that country. We now have 07 branches & booths and 08 ATMs including 2 at off-site locations. While digital omnipresence serves one group of customers, physical presence serves another. We are redefining convenience and providing multiple options to all our valued customers.

# CREATING VALUE WITH ACCOUNTABILITY AND TRANSPARENCY

Enterprise Governance, an emerging term in the post-Enron era that combines corporate governance or conformance and business governance or performance, encapsulates all the factors that go into governing of an organisation. The two dimensions are indispensable to one another. Commercial Bank has a balanced focus on both dimensions.

The Bank is firmly committed to the highest standards of corporate governance and has complied with the majority of good corporate governance practices recommended by various regulatory bodies such as The Institute of Chartered Accountants of Sri Lanka, Central Bank of Sri Lanka etc. As your representatives, the Board of Directors ensures that the activities of the Bank are at all times conducted with the highest ethical standards and in the best interests of all its stakeholders.

The Board of Directors sets the strategic direction and guides the corporate

values. It has set up and enforces clear lines of responsibility and accountability throughout the Bank; as summarized in the diagram below.

The Board on its part has an Audit Committee, Personnel & Remuneration Committee, Credit Committee, Corporate Planning Committee and Pension Reforms Committee. The composition, mandate and workings of these committees are elaborated on succeeding pages of this section.

Creating value for shareholders through performance with the rest of the staff is the responsibility of the Corporate Management. Each function/profit centre is headed by a member of the Corporate Management. Key Performance Indicators (KPIs) of each function/profit centre as per the corporate plan and the budget are reviewed periodically.

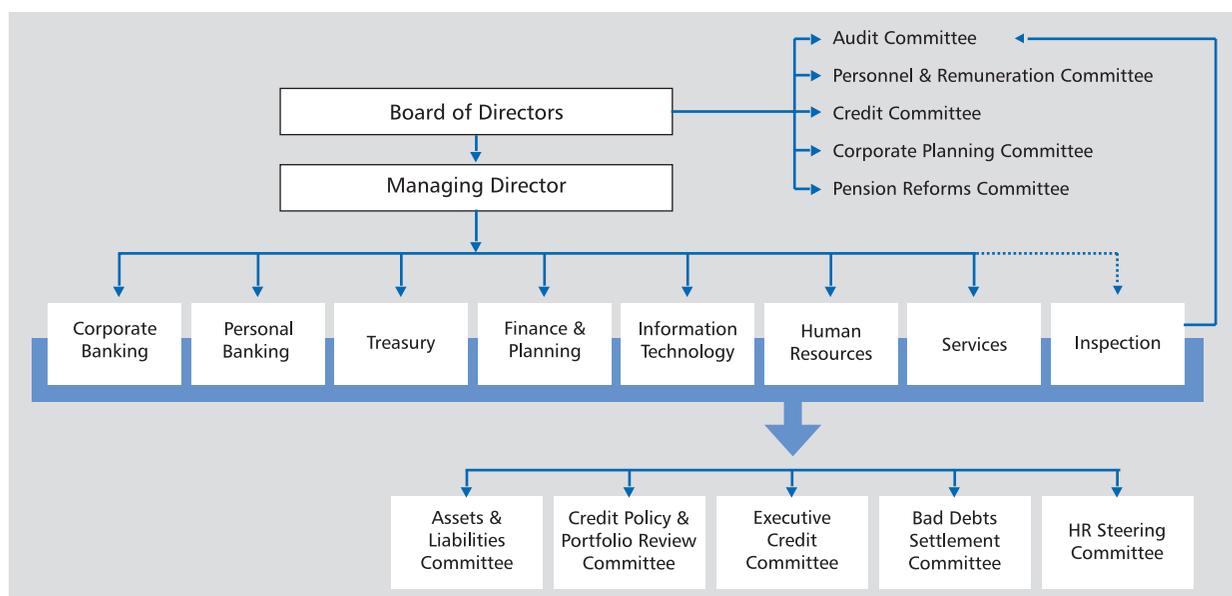
In addition the Bank has cross functional management committees as

also shown in the diagram below. These committees are made up of members from both Corporate Management and Senior Management of the Bank. These committees too meet frequently and review the level of achievement of KPIs.

Empirical evidence shows that well governed companies perform better. The Bank has been able to record an excellent performance as evident from the Compounded Annual Growth Rates of 25% in business volumes and 21% in profits in the past decade.

The performance aspect of Enterprise Governance and the management of risks in the process are dealt with in detail in the Management Discussion and Analysis and the Risk Management chapters shown elsewhere in this Annual Report.

The table on page 65 demonstrates the manner and the extent to which the Bank adheres to good corporate governance principles.



Corporate Governance Principle	Manner and Extent of Adherence
<b>Directors</b>	
<b>Board</b>	
Composition of the Board	Board comprises of eight Non-Executive Directors of whom three are nominee Directors and one Executive Director who is the Chief Executive Officer. They encompass a range of talents, skills and expertise required to provide sound and prudent guidance with respect to the operations and interests of the Bank
Holding of regular Board meetings	Regular Board meetings are held monthly while special Board meetings are convened whenever necessary. In addition, there are several Board sub-committees, details of which are given on page 72.
Availability of formal schedule of matters specifically reserved to the decision making of the Board	<p>Board is responsible for:</p> <ul style="list-style-type: none"> <li>● Ensuring satisfactory performance as representatives of the shareholders</li> <li>● Deciding on the strategic direction of the Bank</li> <li>● Formulation of policies and strategies and monitoring successful implementation thereof</li> <li>● Appointment of the CEO, approving the organisational structure and planning for succession of Corporate Management</li> <li>● Ensuring the implementation of an effective internal control system</li> <li>● Ensuring compliance with the highest ethical and legal standards</li> <li>● Ensuring that a proper risk management system is in place</li> <li>● Approval of credit facilities beyond the delegated authority of the Executive Credit Committee</li> <li>● Deciding on major capital investments on acquisitions and expansions</li> <li>● Approval of the budget and the corporate plan</li> <li>● Approval of annual and interim financial statements for publication</li> </ul>
Procedure for the Directors to obtain independent professional advice	Board sub-committees advise the Board on various matters under their purview. In addition, the Board obtains independent professional advice from external sources whenever the Board deems it necessary
Company Secretary	An Attorney-at-Law functions as the Secretary of the Board. She ensures that proper Board procedures are followed and that applicable rules and regulations are adhered to. She minutes all the proceedings at the Board meetings under the supervision of the Chairman who signs the minutes at the subsequent meeting
Independent judgement	Directors are committed to add value and bring independent judgement to bear on the decision making process of the Bank, and to carry out their duties free from any undue influence or control of other parties
Dedication of adequate time and effort to matters of the Board and the Company	Board dedicates adequate time to the matters of the Board and the Bank. In addition to attending the regular monthly Board as well as Board sub-committees meetings, matters are also referred to them by circulation
Training for the Directors	Advice is sought from independent experts and presentations are made to the Board whenever major changes affecting the banking industry are announced
<b>Chairman and CEO</b>	
Clear division of responsibilities in running the Board and executive responsibilities of running the Bank's business	Positions of the Chairman and the CEO are separated, thereby preventing unfettered powers for decision making in one person. Chairman is a Non-Executive Director while the CEO is an Executive Director
Presence of a strong and independent non-executive element on the Board	Majority of the Directors are Non-Executive independent Directors

Corporate Governance Principle	Manner and Extent of Adherence
<b>Chairman's Role</b>	
Conducting Board proceedings in a proper manner	Chairman conducts Board meetings ensuring effective participation of all the Directors, heeding to their concerns and maintaining the balance of power. The Board is in full control of the Bank's affairs
<b>Financial Acumen</b>	
Financial acumen of the Board	There are two senior Chartered Accountants, one Chartered Management Accountant and one Chartered Financial Analyst in the Board who offer guidance on matters relating to finance
<b>Board Balance</b>	
Balance of the Board	Majority of the Directors are Non-Executive independent Directors. The Banking Act No. 30 of 1988 prior to the amendments in 2005 had provisions restricting employees of a bank other than the CEO being appointed as Directors of that bank. However, the amendments to the Banking Act in 2005 provide for up to one-third of the Board members to be appointed from employees as Executive Directors. At present, only the CEO is in the Board as an Executive Director. The Board believes that the combined knowledge and experience of the Board matches the strategic demands facing the Bank
<b>Supply of Information</b>	
Availability of quality management information	A well-streamlined Management Information System is in place. Accurate and relevant information relating to matters referred to the members of the Board are made available to them well in advance. Whenever, the Board finds that the information made available to them for a decision is insufficient, they call for additional information and the Chairman ensures that all Directors are properly briefed on the matters deliberated on at the meetings
<b>Appointments to the Board</b>	
Availability of a Nomination Committee for making recommendations on all new Board appointments	The Bank does not have a Nomination Committee for making recommendations on appointments to the Board. The CEO is appointed by the Board. In terms of the Articles of Association, each shareholder holding a block of shares representing 12% of the Bank's issued voting share capital is entitled to appoint a Director, subject to a maximum of two Directors, provided that the shareholder has obtained the prior approval of the Monetary Board of the Central Bank for the shareholding and the consent of the Board of Directors of the Bank for nominating rights, which may or may not be given at the sole discretion of the Board. Accordingly, two major shareholders viz. the DFCC Bank and the IFC have the right to appoint two Directors and one Director, respectively (nominee Directors). Appointment of any other new Director is made with the consent of all the Directors and such new Director retires by rotation at the first opportunity after his appointment and offer himself for re-election.
Disclosure of details of new Directors to shareholders	Details of new Directors are made available to the shareholders on their appointment. Prior notice on appointment of new Directors is given to the Director of Bank Supervision
<b>Re-election</b>	
Re-election of Directors	Except for the CEO and the three nominee Directors, the Memorandum and Articles of Association provide for one third of the remaining Directors to retire by rotation each year. They are however, eligible to be reappointed by the shareholders at the Annual General Meeting. Though the nominee Directors are not subject to retire by rotation, the Board is entitled to remove any such Director, if they are of the opinion that such removal is in the best interest of the Bank provided that the shareholder concerned is entitled to nominate another person as the nominee Director. The profiles of all the Directors are given on page 10 of the Annual Report

Corporate Governance Principle	Manner and Extent of Adherence
<b>Appraisal of Board Performance</b>	
Appraisal of Board performance	<p>The Board has implemented a self-assessment exercise covering key functions under the following activities to assess the performance of the Board and carries out the evaluations annually:</p> <ul style="list-style-type: none"> <li>● Discharge of statutory/regulatory duties and Board responsibilities</li> <li>● Corporate Governance and Risk Management monitoring</li> <li>● Seeking and contributing views and opinions on strategic decision making</li> <li>● Leveraging the skills, expertise, contacts of individual Board members in furtherance of business</li> <li>● Understanding the compensation philosophy - “to retain and motivate staff in a manner appropriate for the business”</li> <li>● Understanding the succession plans to ensure comprehensive staff succession - “to ensure talent availability and address expectations of high potential and high quality staff”</li> <li>● Overall view of Management of the business by the Board of Management</li> </ul> <p>Non-Audit Committee Board members assess the performance of the Board Audit Committee</p>
<b>Appraisal of the CEO</b>	
Appraisal of the CEO	<p>The Board sets financial and non-financial goals and objectives for the CEO in line with the short, medium and long term goals of the Bank and has delegated appropriate authority to the Management to implement strategic objectives of the Bank. The CEO is entrusted with the Management of the Bank's operations and he is fully accountable to the Board. The main corporate goals and objectives emanating from the Bank's Corporate Plan and the Budget are incorporated as personal goals of the CEO, whose performance is assessed by the Chairman annually and the assessment is ratified by the Board</p>
<b>Directors' Remuneration</b>	
<b>Remuneration Procedure</b>	
Policy for Directors' Remuneration	<p>Based on the performance appraisal, the remuneration package of the CEO is determined by the Board. The remuneration package of the other Directors is determined in accordance with the international practices</p>
<b>Level and Make Up of Remuneration</b>	
Determination of the level of remuneration of both Executive and Non-Executive Directors	<p>A sufficiently attractive remuneration package is offered to both the CEO and the Non-Executive Directors in order to attract and retain them. With the approval of the shareholders, the Bank established an Employee Share Option Plan in 2002 for the benefit of its senior executives, under which options are offered over a period of four years at the rate of 1.25% of the issued voting share capital. The CEO is entitled for options. The eligibility and the number of options allotted are based on the Bank's overall performance and the achievement of individual targets. The prices of the options are determined at the average market prices of the voting shares during the last three months of each year. Non-Executive Directors are not eligible for options under this ESOP</p>
<b>Disclosure of Remuneration</b>	
Disclosure of remuneration to the Board as a whole and a statement in the Annual Report on the policy adopted in remuneration	<p>The remuneration of the CEO and the Non-Executive Directors is disclosed in this Annual Report</p>

Corporate Governance Principle	Manner and Extent of Adherence
<b>Relationships with Shareholders</b>	
<b>Constructive use of the General Meetings</b>	
Building up relationships with shareholders	The Bank always welcomes active participation of the shareholders at the General Meetings and solicits their views at all times, thus promoting a healthy dialogue. Whenever possible, the Bank implements their suggestions
Making available the Notice of Meeting, related documents and a summary of the procedures governing voting at the general meetings	21 clean days notice is given to the shareholders in terms of the provisions in the Companies Act and the Memorandum of Association of the Bank. A summary of the procedures governing voting at the general meetings is given in the Proxy Form
Enhancing shareholder value	The market capitalisation of the Bank's shares stood at Rs. 26.196 billion, as at December 31, 2006, (which was the highest market capitalisation among all financial institutions in the country), an increase of 41.40% compared to the previous year end. A dividend of 50% has been proposed for 2006. The Board of Directors at a special Board meeting held on January 31, 2007 proposed a rights issue of ordinary shares on the basis of three new shares for ten existing shares to be followed by a scrip issue of ordinary shares on the basis of one ordinary share for every three existing shares on the enhanced share capital of the Bank consequent to the rights issue, subject to the approvals of the Colombo Stock Exchange and the shareholders of the Bank. These bear ample testimony to the Bank's concerted efforts at enhancing shareholder value.
<b>Major Transactions</b>	
Disclosure of major transactions and their impact on the consolidated net assets of the Company	Done where relevant. During the year 2006, the Bank restructured its Pension Scheme from a defined benefit plan to a defined contribution plan and the initial cost of such restructuring amounting to Rs. 1.654 million was debited to the Income Statement. There were no other major transactions that materially affected the Bank's net assets base.
Disclosure to the shareholders if the value of a major transaction exceeds half the value of the Company's net assets or that of a subsidiary, which has a material impact on consolidated net assets of the Company, prior to committing for such transaction	Done where relevant. However, the Bank has not engaged nor committed for such transactions in the recent history of the Bank.  As mentioned in the Chairman's Review the Board of Directors announced its decision to explore the feasibility of merging the Bank with the NDB bank, if the proposed merger takes place and the value of the transaction exceeds one half the value of the net assets of the Bank, necessary disclosures will be made prior to committing for such transaction.

Corporate Governance Principle	Manner and Extent of Adherence
<b>Accountability and Audit</b>	
<b>Financial Reporting</b>	
Disclosure of an assessment on the position and prospects of the Company	Bank attaches high priority to timely publication of quarterly and annual results with comprehensive details far in excess of the statutory requirements, enabling both existing and prospective shareholders to make a timely and fair assessment of the Bank's performance and prospects and informed decisions. Mediums of publication include printed materials, newspapers and the web site of the Bank. We strictly adhere to the accounting formats and other procedures laid down by the regulatory authorities such as the Central Bank and the Colombo Stock Exchange, in the submission of all periodic returns and other information. Price sensitive information is released to the regulators on a timely basis. The financial statements are prepared in accordance with the Sri Lanka Accounting Standards, which are based on the International Accounting Standards. Therefore, the Bank's financial statements comply with the International Accounting Standards in all material respects, to the extent that International Accounting Standards have been adopted in Sri Lanka.
Annual Report should contain a declaration by the Directors	Directors' Report is given on pages 87 to 91 of this Annual Report
Presenting a statement setting out the responsibilities of the Directors for financial statements and a statement by the Auditors about their reporting responsibilities	The Statement of Directors' Responsibility for Financial Reporting is given on page 92 of this Annual Report. Auditors' Report on the financial statements of the Bank for the year ended December 31, 2006 is given on page 95 of this Annual Report
Presenting a Management Report in the Annual Report	This is given under the Management Discussion and Analysis on pages 21 to 36 of this Annual Report
Declaration by the Board as to whether the business is a going concern	This is given in the Directors' Report on page 91 of this Annual Report
Summoning an EGM to notify the shareholders if net assets fall below one half of the shareholders' funds	There have not been such situations in the past. However, should the situation arise an EGM will be called for and shareholders will be notified

Corporate Governance Principle	Manner and Extent of Adherence
<b>Internal Controls</b>	
Maintaining a sound system of internal controls covering financial, operational, compliance and risk management to safeguard shareholders' investments and the Company's assets	Directors have put in place effective internal control, risk management and compliance systems to ensure that no legal, banking, company, stock exchange and other regulations are violated. A summary of the risk management measures in place at the Bank is given on page 76 of this Report. In addition, an Integrated Risk Management Department to address all major risks faced by the Bank is being setup with the expertise from the Deutsche Bank, Asia Pacific Head Office, Singapore
Reviewing of the effectiveness of internal controls periodically by the Directors and reporting thereon to the shareholders	The effectiveness of the internal control systems is periodically reviewed by the Board Audit Committee and major observations are reported to the Board. It also ensures that effective internal and external audit procedures are in place and these functions are carried out by the Inspection Department which is ably assisted by five firms of Chartered Accountants approved by the Central Bank of Sri Lanka. The Board reviews the reports arising from the internal and external audits and monitors the progress of the Bank by evaluating the results against the budget and the industry performance
<b>Audit Committee and Auditors</b>	
Availability of an Audit Committee comprising of independent Non-Executive Directors and reporting thereon in the Annual Report	An active Board Audit Committee headed by the Deputy Chairman and represented by two other Non-Executive Directors is in place. The Managing Director attends the meetings by invitation. The Committee met four times during the year. The full report of this Committee including the terms of reference and specific tasks carried out during the year is given on page 94 of this Annual Report
Maintaining appropriate relationships with the External Auditors to ensure their objectivity and independence	Bank maintains appropriate relationships with the External Auditors, M/s. Ernst & Young. During the year, provision of non-audit services to the Bank by them was limited to tax consultancy work
<b>Employees/Other Stakeholders</b>	
Rights of Employees/ other stakeholders	Bank respects the rights of all the stakeholders whether established by law or otherwise. Stakeholders have access to relevant, sufficient and reliable information on a timely and regular basis thus safeguarding the interests
	Majority of the Executive staff of the Sri Lankan Operations other than the Corporate Management of the Bank are members of either the Executive Officers' Association or the Staff Association while all other permanent staff are members of the Ceylon Bank Employees' Union. Employees and their representative bodies are given unrestricted access to the Management as well as to the Board to voice their concerns about any illegal or unethical practices without compromising their rights in any way
	Several employee performance-enhancing mechanisms such as performance appraisal, Employee Share Ownership Schemes and training staff locally as well as overseas are in place. Bank periodically conducts employee satisfaction surveys. The last such survey was conducted in 2005 and the survey results have been made available to members of the staff
	By maintaining Liquid Assets and the Capital Adequacy Ratios above the minimum statutory requirements and by constantly monitoring the risk profile, the Bank ensures its liquidity and solvency

Corporate Governance Principle	Manner and Extent of Adherence
<b>Corporate Governance</b>	
Disclosure of good corporate governance practices adopted in the Bank	<p>In order to further strengthen the good corporate governance practices already in place in the Bank by identifying the latest best practices around the world and implementing them wherever gaps are found, we periodically evaluate our practices vis-à-vis the OECD Principles of Corporate Governance, which is acknowledged world over as an important initiative in this sphere, the Code of Best Practice on Corporate Governance issued by The Institute of Chartered Accountants of Sri Lanka and the Code of Corporate Governance for Banks and Financial Institutions issued by the Central Bank of Sri Lanka</p> <p>We are happy to note that majority of the principles and practices recommended in these codes are already in place in the Bank. A few of the practices not found to be in place in the Bank have been identified and corrective actions are being taken. We also believe that the amendments made to the Banking Act and the proposed amendments to the Companies Act will improve the legal infrastructure and the regulatory framework relating to Corporate Governance of the Bank</p> <p>We believe that the various accolades conferred on the Bank such as the Annual Report 2005 of the Bank being selected as the Winner of the inaugural Corporate Governance Disclosure Award by the South Asian Federation of Accountants and the AA+ (lka) rating being reaffirmed by Fitch Ratings Lanka Ltd. are, inter alia, an acknowledgement of the good corporate governance practices adopted by the Bank.</p> <p>Extent to which the Bank has complied with the good Corporate Governance principles is given as above in this report</p>

There are several Board sub-committees, each with a defined scope of work and terms of reference. These committees are responsible for providing independent and expert advice to the Board on the subjects assigned.

The Board sub-committee on Corporate Planning provides guidance on the formulation of the Bank's Corporate Plan. In addition, all the members of the Board of Directors deliberate on the Corporate Plan and the Budget at special Board meetings. This process helps the Board to focus on the strategic direction and to identify its implications on all the areas of the business. Implementation of the strategy and its ongoing relevance and success is then assessed on a regular basis.

The composition, scope/principal activities carried out during the year and the number of meetings held and attendance by the respective members of the different Board sub-committees are given below.

Board Sub-Committees			
Committee/ Composition	No. of Meetings		Scope of the Sub-Committee/Principal Activities carried out during the year
	Held	Attendance	
<b>Audit</b>			
B.R.L. Fernando *	4	4	Ensuring that a sound financial reporting system is in place in conformity with the rules, regulations and ethical guidelines. Full Report of this Committee detailing the activities undertaken during the year is given on page 94  In addition to the Board members, Mr. A.T.P Edirisinghe, a practising Chartered Accountant in the capacity of a consultant also attended all four meetings by invitation to provide expert advice to the Committee
A.L. Gooneratne <i>(by invitation)</i>	4	4	
Dr. H.S. Wanasinghe	4	4	
A.N. Fonseka	4	4	
<b>Personnel &amp; Remuneration</b>			
M.J.C. Amarasuriya *	2	2	Maintaining a market oriented remuneration policy for the Bank's staff, enabling the Bank to attract the best personnel in the market while maintaining a contended staff and making recommendations to the Board on appointments to the Corporate Management and their succession planning Full Report of this Committee is given on page 93  Bank obtained the services of Hewitt Outsourcing Services (India) Ltd. to conduct a Salary Survey in order to ascertain the market levels of salaries and other remuneration which were taken into consideration in granting salary increases to the Executive staff
A.L. Gooneratne	2	2	
Dr. H.S. Wanasinghe	2	2	
L.J.A. Fernando	2	2	
D.S. Weerakkody	2	2	
<b>Credit</b>			
M.J.C. Amarasuriya *			Formulating the Bank's Credit Policy and monitoring the Bank's Credit Risk. Approving the facilities referred to the Committee within its Delegated Authority. During the year, the Committee did not meet but approved the facility papers by circulation
B.R.L. Fernando			
A.L. Gooneratne			
<b>Corporate Planning</b>			
M.J.C. Amarasuriya *			Ensuring that a proper planning procedure is in place and striving to promote a target driven culture within the Bank. All the members of the Board deliberated on the Corporate Plan and the Budget 2007-2011 at a special Board meeting held in December 2006
A.L. Gooneratne			
A.N. Fonseka			
L.J.A. Fernando			
<b>Pension Reforms</b>			
B.R.L. Fernando *			Making recommendations to the Board on pension reforms. During the year, the Committee did not meet. However, the Board of Directors evaluated the proposals put forward by Hewitt Outsourcing Services (India) Ltd. to restructure the Pension Scheme and approved the implementation of the restructured scheme.
A.L. Gooneratne			
A.N. Fonseka			

\* Chairman of the Committee

# NEW WINDOWS OF OPPORTUNITY

Commercial Bank continued to invest in Sri Lankan people to empower them and open new windows of opportunity. Having pioneered 'triple bottom' line reporting in this country we continue with our practice of reporting on the impact of our activities on the larger community.

In 2004, we established the Commercial Bank Social Responsibility Trust (CBSRT) with a seed contribution of Rs. 25 million and every year the Bank adds up to one per cent of its post-tax profits into the Trust. The goal of the Trust is not to just make disbursements of money but to provide avenues and inspiration for underprivileged communities to take responsibility for their lives and create sustainable livelihoods. A Board of Trustees administers the CBSRT and decides on the projects to be implemented.

Last year we focused on five broad areas of community life: Education, Irrigation, Rebuilding lives after the tsunami, The Differently Abled and Health Care.

## Educating the Next Generation

One hundred university students received scholarships from the Bank last year. Each student will receive Rs. 2,500/- every month for 10 months of the calendar year during the period

of study in the university. The beneficiaries were chosen in collaboration with the University Grants Commission using the criteria adopted by the Mahapola Trust Fund to select students for Mahapola Scholarships.

The number of Advanced Level attempts, parental income, the number of school going children in the family and the distance between home and university were some of the criteria applied in selecting the students. Our aim was to ensure that we selected the most deserving beneficiaries.

The CBSRT Fund will disburse Rs. 2,500 million annually under this initiative.

The Bank continued to reward outstanding academic performance at the Year 5 Scholarship examination. Every year students with a Commercial Bank Arunalu Minor's Savings Account who end up within the top five of the Year 5 Scholarship examination in their respective schools are eligible for prizes. Rs. 10,000/-, 7,500/-, and 5,000/- are given to the top performing students.

In 2006, 184 students received prizes under this scheme and the CBSRT paid out Rs. 1.35 million. The Arunalu saving scheme was launched in 1998 with a view to encouraging the savings habit among school children.



1. An undergraduate receives a Bank scholarship from the Hon. Prime Minister.
2. A top, year 5, Arunalu Account holder receives his prize.
3. Assisting the Peter Weerasekara Children's home

### Sustaining Livelihoods and the Nation

In 2005, the CBSRT initiated a project to restore dilapidated irrigation tanks in different parts of the country. This initiative reflects our overall approach to corporate social responsibility: empowering communities, sustaining livelihoods, participation of beneficiaries and minimum disruption of existing patterns of existence.

Last year we restored and replenished the fourth tank - Udahinguru Wewa in the Anuradhapura District providing fresh opportunities to farmers and families in that locality. In 2005, the Bank restored three tanks in the Kurunegala District.

The restoration project entailed a removal of silt from the tank beds, rebuilding and raising the tank bunds, restoration of sluice gates and the construction of the necessary water distribution systems.

Farmer organisations were actively involved in the restoration process. Not only did it bring down the costs but also helped establish a sense of ownership and belonging in the initiative. Wherever possible the Bank sought to involve beneficiary communities in the design and execution of the project.

These four tanks were restored in two districts where the families are heavily dependent on agriculture for

their livelihood. The Bank has a heavy presence in the area and we believe that it is our responsibility to invest in the future of the communities who live and work in that region.

### Rebuilding Lives after the Tsunami

The Bank continued with its efforts to help those affected by the tsunami. In 2005, the Bank had made a significant contribution to staff affected by the tsunami and to other affected families.

Last year 10 families in the Matara District were provided with new houses from the CBSRT. The houses were built on the lands owned by the recipients or on lands provided by the State.

Each house is approximately 500 square feet and comprises two bedrooms, a sitting room and other essentials along with a small garden. The Bank hopes that these new

houses will help the families recover from the trauma and recommence their lives with renewed hope.

### Inspiring the Differently Abled

The Bank continued to work with the differently abled in an effort to inspire and build self-confidence among this segment of the population.

In December 2006 too, the Bank held a special programme for the disabled from the Cheshire Home in Mount Lavinia. The programme consisted of an entertainment segment and a 'motivational' segment.

The Bank believes that the differently abled have a vital role to play in the society and will continue to assist them to explore their talent and ability. Our Reid Avenue Branch



At the restored Udahinguru Wewa in Anuradhapura



Sponsoring R.S. Kalugampitiya of Vidyarthi College, Kandy to the 37th world Chess Olympiad.

has been specially tailored to the differently abled and the Bank is making a strong effort to ensure that our ATMs, Mini-Coms and Branches are all sensitive to the needs of this group.

The CBSRT Fund also made a contribution to the Sri Lanka Federation for the Visually Handicapped (SLFVH). The SLFVH is currently involved in a number of projects including the construction of hostels for blind elders in Tangalle and Hambantota and the setting up of handloom weaving centres.

### Improving Health Care Facilities

The Bank assisted the Handy Memorial Trust to upgrade two Cardiology Units at the National Hospital last year. The Handy Memorial Trust, set up in the name of one of the country's pioneer

cardiologists, regularly maintains and upgrades the cardiology facilities at the National Hospital.

At the request of the Karapitiya Hospital Development Society the CBSRT provided a Public Address System to the hospital and installed it in the hospital premises with the assistance of the technical staff of the Bank.

### National Vesak Festival

Once again, the Bank helped with sponsorship of the National Vesak Festival. Last year's festival was special because it was the 2550th year in the Buddhist calendar and special efforts were made to mark this event with grandeur.

### The 10th South Asian Games

Last year saw Colombo hosting the 10th South Asian Games, one of the largest sporting events ever held in

this country. The Bank's CBSRT was proud to have been associated with this event and made a contribution of Rs. 2,000 million towards the costs.

### Green Loans

While we engage in a number of activities towards the direct empowerment of communities, part of the Bank's loan portfolio is directed at creating cleaner and greener environments.

For many years we have tried to promote industries that control pollution and emissions, adopt safer practices at the workplace and consider alternative energy sources. We continued with this in 2006. The E-Friends-II Loans scheme provides credit at a concessionary interest rate of 6.5% p.a. to industries that adopt E-friendly practices.



Inaugurating the Bank sponsored Public Address System in Karapitiya Hospital.



Handing over a donation for the blind elders' home, Walasmulla.

# MANAGING OPPORTUNITY WITH PRUDENCE

## Relationship between Risk, Return and Gearing

Banks make money by taking risks and properly pricing them. Therefore, risk is an essential ingredient in the management of a bank and risk taking must be informed and prudent. Risk management is thus increasingly becoming a core function of a bank.

The International Standards Organisation defines **RISK as the combination of the probability of an event and its consequences**. While risk is prevalent in different forms and magnitudes in any organisation, its ramifications for an organisation in the business of financial intermediation are wide and deep. Majority of the risks that banks face has an upside as well which makes risk management a rewarding discipline.

An effective risk management framework helps banks in their attempts to achieve the optimum trade-off between risks and returns. On one hand, shareholders demand an acceptable return on their equity. On the other hand, the return on assets of banks is relatively lower compared to that of other businesses due to the thin margins the banks are operating on. The way out for banks to address this dilemma is to operate at high levels of gearing. However, due to the positive correlation between risk and return and the highly volatile political, economic, social and technological environment, high levels of gearing

may lead to a deterioration in the risk profile of the banks.

Undoubtedly, capital which is the primary means of protection against the risk of insolvency is fast becoming the 'limiting factor' for banks and as such, capital management of banks is gaining more and more significance. It is all about directing this scarce resource to the opportunities that are expected to generate the maximum return with the minimum risk. An effective risk management framework can make an immense contribution in the efforts of the banks in managing the available capital.

## Broad Risk Exposures

Like any other player in the financial services industry, the Bank is exposed to a multitude of risks which can broadly be classified into **Credit, Market, Asset & Liability Management and Operational Risks**, as detailed below.

### Credit Risk

Credit risk is most simply defined as the potential that a borrower or a counterparty will fail to meet its obligations in accordance with agreed terms and conditions. This includes non-repayment of capital and/or interest within the agreed time frame, at the agreed rate of interest and in the agreed currency.

### Market Risk

Market risk is the risk of loss resulting from changes in market driven factors such as interest rates, foreign currency exchange rates, equity prices and commodity prices.

### Asset & Liability Management Risk

This is the risk that arises to a bank from the mismatches in various attributes of its assets and liabilities such as non-alignment of maturities (in the case of fixed interest rates) and repricing dates (in the case of variable interest rates) and when the resulting movements in their relative values due to changes in general market factors are not in tandem.

### Operational Risk

Operational risk is defined as the potential loss arising from a breakdown in a bank's, systems and procedures, internal controls, compliance requirements or corporate governance practices, that results in human error, fraud, failure/delay to perform or compromise of the bank's interests by employees. Operational risk also includes the potential loss arising from a major failure of computer systems and from both natural and man-made disasters.

### Risk Management - a rapidly evolving discipline

Continuous advances in technology, developments in the regulatory processes world over, growing

complexity and sophistication of products and services offered and the growth in business volumes have all made a fully-fledged independent risk management function an imperative for a bank. Advances in technology coupled with competition and customer demands are forcing the banks to adopt more sophisticated systems for processing transactions and for offering efficient customer service. Regulatory developments are making it compulsory that the banks implement more rigorous risk management methodologies in its internal models. On the other hand, Basel II Accord places heavy reliance on the internal risk assessment and management techniques for the purpose of quantifying and allocating capital for credit, market and operational risks. Regulators will be gradually moving from 'compliance' based supervision to 'risk' based supervision by placing more and more emphasis on the soundness of the risk management practices of banks.

Techniques for the measurement and management of risks continue to evolve in response to the above developments. Banks that wish to remain competitive and generate the maximum return commensurate with their risk profiles to the shareholders must keep up with these evolving techniques. A successful risk management function can help banks meet many of these challenges by providing a framework for managers

to explicitly consider how risk exposures are changing, determine the amount of risk they are willing to accept and ensure that they have the appropriate risk mitigants and controls in place to align the risk to target levels of risk appetite.

### **Managing Risk at Commercial Bank**

A wider array of risk management tools and practices is available for financial institutions today. However, the design of the risk management system at Commercial Bank is bank specific and depends on its size and the level of sophistication. It is structured to address both banking as well as non-banking risks in both on-balance sheet and off balance sheet exposures, with a view to protecting capital and enhancing shareholder value. The risk management system ensures that the Bank takes well-calculated business risks while safeguarding the Bank's capital, its financial resources and profitability from various risks. While trying to eliminate, if possible, certain risks altogether, such as legal and operational risks, the Bank is also mindful of the correlation between risk and reward in other areas. It is the Bank's policy to manage such risks effectively so as to mitigate or minimise such risks and to maximise the return to all its stakeholders. In this regard, the Bank has recognised the fact that continuing development

of the risk management infrastructure in terms of systems and procedures and the necessary skills and expertise among the relevant staff to handle these risks professionally is the most effective strategy and consequently allocated sufficient resources for developing such skills. The management continues to oversee and update the systems, policies and procedures in all dimensions of operations within the broad guidelines and policies set by the Board. These policies and procedures are integrated into the day-to-day decision making and corporate governance process.

The total assets portfolio of the Bank reached Rs. 223.974 billion (US \$ 2.083 billion) by end 2006. Apart from its domestic and off-shore banking operations in Sri Lanka and in Bangladesh, Bank is planning to expand its activities in the other SAARC countries with a view to realising its Vision of having an international presence by the year 2011 and also, to offer other banking services such as money remittances in certain countries in the Middle East, Europe and North America. Regulatory authorities in various countries place heavy reliance on the strength of the risk management measures in place at the banks as a qualification criterion when assessing the applications for setting up operations in overseas locations.

## Risk Management

Rapid growth that the Bank has been experiencing over the past several years has exerted considerable pressure on many spheres of the Bank including capital, systems and procedures, management information systems, maintenance of asset quality, asset-liability management etc. The Bank believes that its continued success depends on its ability to prepare for unexpected and potentially much less favourable, events and outcomes and is making the necessary arrangements to address these issues.

### Board and Management Oversight

The Board of Directors and the Management provide important oversight to risk management practices of the Bank resulting in proper alignment of its strategies with the risk appetite of the Bank and proper deployment of capital, in its efforts to create value for all the stakeholders. Board of Directors at its meetings and through various sub-committees such as the Board Audit Committee and the Board Credit Committee and the Management at the Executive Committee and various sub-committees such as the Executive Credit Committee, the Credit Policy and Portfolio Review Committee and the Assets & Liabilities Committee make a substantial contribution in these efforts.

During the year, all sectional heads at the Management level of the Bank continued to periodically assess the extent of implementation of various risk management measures against each risk in a wide-ranging list of possible banking and non-banking risks documented. A report thereon was submitted to the Board through the Board Audit Committee as at June 30, 2006 and December 31, 2006, apprising the Board of the most significant risks and actions taken by the Management to manage such risks.

To ensure the effectiveness of the Bank's risk management measures, strict audits were also conducted by the Inspection Department as at March 31, 2006 and September 30, 2006. The independence of the Inspection Department is assured by the Bank's organisation structure.

### 2006 - An Eventful Year

In the backdrop of the above developments, 2006 was an eventful year for the Bank even in the sphere of its risk management infrastructure. The Bank embarked on a project to upgrade its Risk Management and Control Systems by establishing an Integrated Risk Management Department with a view to managing **growth, profitability and capital adequacy** more proactively. An integrated approach would be the most suited since the Bank cannot

view and assess risks in isolation due to the possibilities of a single transaction triggering a number of risks and different business units having exposures to the same customer/counterparty.

An agreement was signed in this regard in June 2006 with the Deutsche Bank, Asia Pacific Head Office, Singapore for obtaining consultancy services. In terms of this agreement, as the first phase, the Deutsche Bank conducted a due diligence on the risk management practices currently in place in the Bank, compared them with the international best practices and submitted a report to the Board of Directors and the Management detailing the gaps observed and their recommendations to address such gaps. The second phase of the project viz. implementation of the recommendations as agreed with the Bank will commence shortly. It is envisaged that the implementation may take about two years before the Integrated Risk Management Department is fully operational. Thereafter, the Bank will be fully geared to manage all the risks of the Bank at all the levels viz. at the transaction level, the business unit level and enterprise-wide.

### Assessment of Riskiness of the Bank's Operations

The Bank estimates its risk exposure based on an internal assessment of the operations and historical data as

well as the market perception to be as follows:

Category of Risk	Rating
Credit Risk	Moderate
Market Risk	Low
Asset & Liability Management Risk	Moderate
Operational Risk	Low

Continuous improvements in asset quality as measured by the Non-Performing Assets Ratio and solvency as measured by net Non-Performing Assets to equity, mitigated the adverse effects, if any, of the Bank's capital position not keeping pace with the Balance Sheet growth and the resulting decline in the equity to assets ratio over the past several years.

### Summary of the Risks, their Implications and Risk Management Measures in place at Commercial Bank

Major forms of Risks faced by the Commercial Bank	Broad implications to the Bank arising from these risks	Important Risk Management measures in place at Commercial Bank to address these risks
<b>Credit Risk</b>		
<ul style="list-style-type: none"> <li>● Default risk</li> <li>● Security risk</li> <li>● Sectoral exposure risk</li> <li>● Legal risk</li> <li>● Related party risk</li> <li>● Counterparty risk</li> <li>● Cross-border risk</li> <li>● Sovereign risk</li> </ul>	<p>Loans and advances is the single biggest asset of the Bank accounting for approximately 67% of the total assets. Hence, credit risk may result in adverse implications on profits arising from suspension of interest and the need to provide for/write off non-performing advances. Increasing non-performing loans ratio may lead to downgrading of the credit rating which may in turn damage the reputation of the Bank. Finally, it may lead to deterioration in the quality of assets</p>	<ul style="list-style-type: none"> <li>● An Intergrated Risk Management Department is being set up</li> <li>● Setting up of an independent Credit Risk Management Unit</li> <li>● Formation of a Credit Monitoring Unit to monitor rescheduling of facilities and classification of overdrafts</li> <li>● Establishing suitable exposure limits for borrowers, lending officers and sectors and monitoring the limits regularly</li> <li>● Risk mitigation steps such as taking collateral</li> <li>● Setting counterparty limits based on financial strength</li> <li>● Training of lending and legal officers on documentation and obtaining professional valuations</li> <li>● Developing skills and expertise in lending officers to scientifically assess project viability and objectively evaluate customer integrity</li> <li>● Educating the staff on provisions in the Banking Act and other relevant statutes and the regulatory guidelines of the Central Bank</li> <li>● Seeking external legal opinion</li> <li>● Prompt action on early warning signals given by the IT system</li> <li>● Strict adherence to the Single Borrower Limit and the regulatory guidelines of the Central Bank on loan classification, interest suspension and provisioning</li> <li>● Maintaining neutrality in politics and arm's length approach in related party lending</li> <li>● Regular review of country situations and country exposures</li> <li>● Overseas expansion to reduce dependance on the Sri Lankan economy</li> <li>● Constant post sanction monitoring with MIS support from the Computer System</li> </ul>

## Risk Management

Major forms of Risks faced by the Commercial Bank	Broad implications to the Bank arising from these risks	Important Risk Management measures in place at Commercial Bank to address these risks
<b>Market and Asset &amp; Liability Management Risks</b>		
<ul style="list-style-type: none"> <li>● Interest rate risk</li> <li>● Liquidity risk</li> <li>● Exchange rate risk</li> <li>● Investment risk</li> <li>● Group financial risk</li> <li>● Share prices declining risk</li> <li>● Country risk</li> </ul>	<p>89% of the assets and 80% of the liabilities are subject to either fixed or variable interest rates. 32% of the assets and 30% of the liabilities are denominated in foreign currencies. Hence, financial/opportunity losses may arise from unexpected movements in market forces. Inability to honour obligations to depositors and other stakeholders on time, may result in breach of contractual obligations and rules and imposition of penalties/reprimanding by regulators. Furthermore, loss of market share, downgrading the credit rating, damages to the reputation and image, loss of employee morale/shareholder confidence, erosion of public confidence, withdrawing or curtailing credit limits by foreign correspondents, may occur</p>	<ul style="list-style-type: none"> <li>● An active Assets &amp; Liabilities Committee (ALCO) that meets fortnightly</li> <li>● ALCO playing an active role in setting policies and monitoring compliance</li> <li>● ALCO decisions are reviewed by the Board</li> <li>● Carrying out gap analysis, timely repricing of products and hedging of exposures</li> <li>● Entering into forward contracts, swapping and currency options</li> <li>● Formulating a Liquidity Management Policy</li> <li>● Daily monitoring of Advances to Deposits Ratio</li> <li>● Maintaining the Liquid Assets Ratio with a contingency buffer</li> <li>● Close monitoring and projecting the trends in the share market</li> <li>● Dealer, broker, counterparty, transaction, product and currencywise exposure limits, which are constantly reviewed</li> <li>● Suitable cut-loss limits on different exposures</li> <li>● Regular monitoring of competitor behaviour and building competitor intelligence</li> <li>● Maintaining strong relationships with the correspondents</li> <li>● Enhancing the fee based income to minimise dependency on fund based income</li> <li>● Timely recognition of market losses through mark to market and exchange revaluation mechanism</li> <li>● Non-engaging in large scale transactions on speculative basis</li> <li>● Non-engaging in large scale derivative transactions</li> <li>● Maintaining open forex positions within 7% of capital funds</li> <li>● Strong access to money markets and credit lines through good reputation, strong earnings, financial strength, credit rating and backing of major shareholders</li> <li>● Segregation of front, mid and back offices at the Treasury</li> <li>● Developing necessary skills and expertise for all areas of the Treasury and setting up IT backed processing systems</li> <li>● Implementation of Software on ALM and Funds Transfer Pricing</li> </ul>
<b>Operational Risk</b>		
<ul style="list-style-type: none"> <li>● Employee behavioural risks such as omission, fraud, judgemental errors, negligence, etc.</li> <li>● Disaster related risks</li> <li>● Trained staff turnover</li> <li>● Insider dealing risk</li> </ul>	<p>Financial losses and damages to reputation arising from breakdowns in systems/procedures and internal controls and disruptions to smooth functioning of the Bank. Resulting deterioration in the quality of customer services. Imposition of penalties/reprimanding by regulators. Loss of competencies over competitors.</p>	<ul style="list-style-type: none"> <li>● Setting up of suitable Delegated Authority levels</li> <li>● Formulation of a succession plan</li> <li>● Creating a conducive working environment for the staff</li> <li>● Training a second layer of staff and signing training bonds</li> <li>● Effective internal audit function</li> <li>● Issuing of circular instructions and protection of sensitive information</li> </ul>

Major forms of Risks faced by the Commercial Bank	Broad implications to the Bank arising from these risks	Important Risk Management measures in place at Commercial Bank to address these risks
<b>Operational Risk (Contd.)</b>		
<ul style="list-style-type: none"> <li>● Sensitive information leakage risk</li> <li>● Lack of creativity and innovativeness</li> <li>● Risk of MIS</li> <li>● IT related risks</li> <li>● Planning &amp; Budget related risks</li> <li>● Shortcomings in the organisational structure</li> <li>● Credit rating falling risk</li> <li>● Money laundering</li> <li>● Changes to statutory requirements</li> <li>● Risk of technological obsolescence</li> <li>● Risk of falling business volumes and market share</li> <li>● Risk of being overtaken and losing the leadership position</li> <li>● Risk of financial disintermediation</li> <li>● Overtrading risk</li> </ul>	<p>Judgemental errors in decision making. Counter actions by the competitors to undermine the Bank's strategic advantages. Hindrances to expansion. Difficulties in maintaining the statutory ratios and sustaining profitability.</p> <p>Financial losses as a result of volatile revenues and reduced profitability. Probability of credit rating being downgraded and the resulting damage to the reputation. Loss of competitiveness and diseconomies of scale may lead to insolvency and ultimately threaten the going concern nature of the business. Overtrading may lead to insufficient capital.</p>	<ul style="list-style-type: none"> <li>● Development of a formal Business Continuity Plan</li> <li>● Setting up of a Business Continuity Management Unit</li> <li>● Quarterly assessment of the extent of compliance with the statutory requirements and reporting to the Board Audit Committee</li> <li>● Obtaining oath of secrecy and certificate of propriety</li> <li>● Building up sustainable competencies</li> <li>● Implementation of computer based MIS System</li> <li>● Implementation of 'Hot Back Up' system</li> <li>● Preventive maintenance of equipment through maintenance contracts with the vendors</li> <li>● Creating awareness on 'Know Your Customer' policy</li> <li>● Building up of contingency buffer in the form of reserves</li> <li>● Implementation of a well planned and sustainable expansion programme</li> <li>● Regular upgrading of hardware and software to keep it 'state-of-the-art'</li> <li>● Inculcating organisational values and ethics in employees</li> <li>● Maintaining a Skills Inventory</li> <li>● Risk transfer measures such as insurance</li> <li>● Innovative and convenient products and services</li> <li>● Offering extended banking hours to customers for their convenience</li> <li>● Regular assessment of the levels of customer satisfaction</li> <li>● Taking prompt action on customer complaints</li> <li>● Periodical review of business strategy, Vision and Mission</li> <li>● Regular assessment of the levels of staff satisfaction</li> <li>● Practising the concept of Management by Objectives through the preparation of a Corporate Plan and an ambitious budget</li> <li>● Monthly review of performance against the budgeted targets</li> <li>● Measuring risk/inflation adjusted performance measures</li> <li>● Establishment of a target driven culture and performance based rewards</li> <li>● Benchmarking with competitor performance</li> <li>● Maintaining a database on competitor intelligence</li> <li>● Promoting customer loyalty</li> <li>● Constantly reminding the staff of the importance of delighting the customer</li> </ul>

### Developments during the year

#### Credit Monitoring Unit

The Credit Monitoring Unit set up in 2004 under the Finance & Planning Division of the Bank in order to avoid conflicts of interests and ensure independence from those responsible for lending, was amalgamated with the Integrated Risk Management Department that is being set up, during the year. The Unit continued to monitor the rescheduling of credit facilities, ensure proper classification of overdrafts and grant permission to branches to monitor non-performing loans beyond one year. The activities of the Unit have immensely contributed to create awareness across the Bank of the guidelines of the Central Bank of Sri Lanka on the subjects and to streamline the related processes.

#### Credit Risk Management Unit

The Credit Risk Management Unit, set up for undertaking an independent assessment of all corporate lending and risk ratings, too was amalgamated with the Integrated Risk Management Department. All credit facilities which were submitted to approving authorities at the levels of the Board Credit Committee and above were first referred to the Risk Management Department for its observations.

#### Treasury Mid-Office

Treasury Mid-Office which was set up for the specific purpose of managing the treasury related risks with a better focus, too will be amalgamated with the Integrated Risk Management Department during the implementation of the recommendations of the Deutsche Bank. The initial objectives of the treasury Mid-Office would include setting up of risk management policies and guidelines, documenting the risk management procedures to be carried out by the Treasury and establishment of required limits and monitoring. The Mid-Office would also be monitoring the liquidity position of the Bank. All Treasury related regulatory and management reporting functions too are expected to be carried out through the Mid-Office.

#### Anti-Money Laundering Efforts

The Anti-Money Laundering (AML) legislation was passed by the Parliament at the beginning of 2006 and came into effect in March 2006. The two pieces of legislation enacted in this regard were the Prevention of Money Laundering Act No. 05 of 2006 (PMLA) and the Financial Transactions Reporting Act No. 06 of 2006 (FTRA). In terms of the FTRA, a Financial Intelligence Unit (FIU) was set up under the purview of the Central Bank of Sri Lanka as the administrative body of the AML regime.

During the year, as required by the directions of the FIU in terms of the provisions in the FTRA, the Bank appointed a senior officer as the Compliance Officer, who is responsible for ensuring the Bank's compliance with the requirements of the Act, to oversee the operation of the AML programme in the Bank and also to liaise with the FIU in all relevant matters.

In terms of the provisions of the FTRA, the thresholds for reporting cash transactions and electronic fund transfers to the FIU fortnightly were set at Rs. 500,000/- and US \$ 5,000 or its equivalent in any foreign currency, respectively. The Bank complied with this requirement with the help of a computer program developed in-house.

Since the FIU is yet to formulate and issue comprehensive regulatory AML guidelines for banks, the Bank was precluded from adopting and operating more comprehensive and documented internal practices in detecting and controlling illegitimate activities, money laundering and terrorist financing. However, the Bank has in fact, already prepared its own document on Anti-Money Laundering policy and procedures, setting out the internal operational guidelines, but awaits finalisation and adaptation until the regulatory guidelines are issued. Nevertheless, the Bank continued to adopt its prudential measures and other safeguards

throughout the year to prevent the use of its systems, products and services for illegal and unlawful purposes.

During the year, the Bank continued to educate its staff adequately on money laundering and terrorist financing activities and the preventive measures in order to prepare them for effective compliance with all the requirements, once the Anti-Money Laundering measures become fully operational shortly.

#### **Software Support for Risk Management**

During the year, the Bank implemented two software modules procured from IPS Sendero, a US based company on Asset & Liability Management and Funds Transfer Pricing. These software are being tested now. The implementation of the modules for the evaluation of profitability, viz. Customer Profitability, Product Profitability and Organisational Profitability will be completed during 2007. Software for credit scoring the personal loans, home loans and credit cards portfolios have been procured and are being tested.

### **Plans for 2007 and onwards**

#### **Integrated Risk Management Department**

Implementation of the risk management measures recommended by the Deutsche Bank to address the gaps observed during the Due Diligence study as explained earlier will receive priority during the year 2007. Emphasis will be given for creating the proper organisation structure to ensure independence of the Risk Management function, upgrading the Risk Management policies and procedures, enhancing the awareness within the Bank of the relationship between risk and return and the importance of the risk management function, upgrading Management Information Systems from a Risk Management perspective and efficient management of the available capital.

#### **Business Continuity Management**

The Business Continuity Management efforts of the Bank are driven by the Business Continuity Management Steering Committee comprising several members of the Corporate Management and the Senior Management. The Steering Committee provides the overall guidance to the Business Continuity Planning (BCP) Committee comprised of senior officers representing all key business and service units of the Bank.

A formal Business Continuity Plan has been developed by the BCP Committee in keeping with the requirements and the guidelines provided by the Central Bank of Sri Lanka and it has been formally approved by the Board of Directors of the Bank. Apart from abiding by the Central Bank requirements, the Bank has identified the need to have a well developed formal Business Continuity Plan which is in par with the industry standards due to the Bank's international presence. The need to address vulnerable operational risks and develop plans to minimise the effects of such risks caused by inadequacies or failures of internal processes, systems and external events including natural disasters has been appreciated and dealt with in the Business Continuity Plan.

In view of the critical nature of the Bank's operations varying from one business unit to another, the Bank's Business Continuity Plan has to be customised to suit each of such business units and business processes. The necessary customisation is underway.

A Business Continuity Management Unit has been set up at a location away from the Head Office in order to provide the necessary operational and logistical support to business units experiencing disruptions and difficulties in managing business operations.

## Risk Management

Awareness programmes have been arranged covering staff of all business units. Special training is being provided to selected staff from the business units to serve in identified teams to handle specified tasks in disaster situations. Through the awareness programs being conducted, it is anticipated that the Bank would be able to create an appropriate BCP Culture among the staff during the current year.

### **Implementation of Basel II Accord**

Basel II Accord is intended to improve the safety and soundness of the financial systems world over by aligning capital adequacy assessment more closely with the underlying risks in the banking industry, providing for a thorough supervisory review process and enhancing market discipline and disclosures. Basel II promises to offer incentives for banks to adopt sound Risk Management practices.

Central Bank announced that the regulatory capital requirements of banks in Sri Lanka will be computed under the Basel II Accord with effect from the first quarter of 2008 while the requirement to maintain capital for the market risk was implemented in 2006. Basel II, once fully implemented will integrate the internal Risk Management systems and regulatory capital adequacy requirements of banks. As required by the Central Bank, during the year 2006, the Bank commenced the computation of Capital Adequacy based on the draft guidelines issued by the Central Bank in terms of the Basel II Accord, on a parallel basis. While the Bank has already made preliminary arrangements for making its systems and procedures Basel II compliant, a lot needs to be done in the ensuing years in this regard. Integrated Risk Management Department, when it is fully operational, will be entrusted with the task of designing and implementing the systems and procedures in this regard. In addition, the Bank will take the required capacity building measures on time to ensure a smooth migration to the advanced approaches of Basel II at the right time.

# Financial Reports

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## Financial Calendar - 2006/07

Final Dividend for 2005 paid on April 6, 2006  
Interim Dividend for 2006 paid on November 14, 2006  
Annual Report and Accounts for 2006 signed on February 15, 2007  
Thirty-Eighth Annual General Meeting to be held on March 28, 2007  
Final Dividend for 2006 proposed to be paid on March 28, 2007

## Interim Financial Statements in terms of Rule 8.3 of the Colombo Stock Exchange and as per the requirements of the Central Bank of Sri Lanka

For the three months ended March 31, 2006 (unaudited) in May 2006  
For the six months ended June 30, 2006 (unaudited) in August 2006  
For the nine months ended September 30, 2006 (unaudited) in November 2006  
Annual Report and Accounts for 2006 (audited) in March 2007

## Proposed Financial Calendar - 2006/07

Interim Dividend for 2007 in November 2007  
Annual Report and Accounts for 2007 to be signed in February 2008  
Thirty-Ninth Annual General Meeting to be held in March 2008  
Final Dividend for 2007 in March 2008

## Interim Financial Statements in terms of Rule 8.3 of the Colombo Stock Exchange and as per the requirements of the Central Bank of Sri Lanka

For the three months ending March 31, 2007 (unaudited) in May 2007  
For the six months ending June 30, 2007 (unaudited) in August 2007  
For the nine months ending September 30, 2007 (unaudited) in November 2007  
Annual Report and Accounts for 2007 (audited) in March 2008



### General

The Directors have pleasure in presenting to the members their Report together with the audited Financial Statements of the Commercial Bank of Ceylon Ltd., a public limited liability company incorporated in Sri Lanka on June 25, 1969 under the Companies Ordinance No. 51 of 1938, quoted in the Colombo Stock Exchange in March 1970 and a licensed commercial bank under the Banking Act No. 30 of 1988, for the year ended December 31, 2006.

These were approved by the Directors on February 15, 2007.

### Principal Activities

#### Bank

The principal activities of the Bank continued to be banking and related activities such as accepting deposits, personal banking, trade financing, off-shore banking, resident and non-resident foreign currency operations, travel related services, corporate and retail credit, project financing, lease financing, rural credit, issuing of local and international debit and credit cards, telebanking facilities, bancassurance, internet banking, dealing in Government securities, bullion trading, export and domestic factoring etc.

#### Subsidiaries

The principal activities of Commercial Development Co. Ltd., X-pertise Ltd. and ONEzero Co. Ltd. are property development, training and development of human resource and providing IT related services, respectively. The operations of the Commercial Bank Primary Dealer Ltd., whose principal activity was dealing in Government securities, ceased its operations as at September 30, 2005, consequent to the Bank obtaining the licence to operate as a Primary Dealer. The proceedings for voluntary winding up of the Company are in progress.

#### Associates

The principal activities of Commercial Leasing Co. Ltd., Equity Investments Lanka Ltd. and Commercial Fund Management (Pvt) Ltd. are leasing and factoring, venture capital and fund management, respectively. However, Commercial Fund Management (Pvt) Ltd., ceased to be an associate company of the Bank with effect from January 23, 2007, consequent to the disposal of the Bank's interest in this Company.

There were no significant changes in the nature of principal activities of the Bank and the Group during the year under review.

### Review of Business

The Chairman's Review on page 4 and the Managing Director's Report on page 13 provide an overall assessment on the financial performance and financial position of the Group, describe in detail its affairs and important events of the year. These reports form an integral part of the Directors' Report.

### Branch Expansion/Future Developments

The branch expansion policy continued during the year and the Bank opened 10 Branches, 3 Customer Service Points (CSPs) and 2 MiniComs and 1 Service Point in Sri Lanka and 2 Branches in Bangladesh. Two CSPs were also upgraded to fully-fledged branches. Bank intends to expand its branch network both in Sri Lanka and in Bangladesh. Further, the Bank launched the first online cheque viewing facility, providing the customers the convenience of viewing the images of cleared and paid cheques issued by them. This facility will be extended to cheques deposited as well in the near future. In addition, the Bank tied up with MoneyGram, the global funds transfer company to further enhance the Bank's e-Exchange money transfer system. The Bank is now able to offer customers of over 104,000 locations in 170 countries, the ability to transfer funds via the Internet.

### System of Internal Controls

The Board of Directors has instituted an effective and comprehensive system of Internal Controls covering financial operations and compliance control and risk management required to carry on the business of banking in an orderly manner, safeguard its assets and secure as far as possible the accuracy and reliability of the records.

### Corporate Governance

Systems and procedures are in place to ensure that Corporate Governance is properly practised. Specific measures taken in this regard are elaborated in Enterprise Governance on page 64 of this Report.

### Human Resources

The Bank continued to implement appropriate Human Resource Management policies and practices to develop its employees and also to ensure their optimum contribution towards the achievement of corporate goals. Specific measures taken in this regard are detailed in the Knowledge Management Report and Community Impact Report on pages 53 and 73 respectively.

### Board Audit Committee

The following Non-Executive Directors of the Board served as members of the Board Audit Committee:

Mr. B.R.L. Fernando (Chairman)  
Dr. H.S. Wanasinghe  
Mr. A.N. Fonseka

Mr. A.L. Gooneratne, Managing Director of the Bank and Mr. A.T.P. Edirisinghe, a practising Chartered Accountant in the capacity of a Consultant attended the meetings by invitation.

The report of the Audit Committee is given on page 94 of this Report.

### Vision, Mission and Corporate Conduct

The Bank's new Vision and Mission are given on page 1 of this Report. The business activities of the Bank are conducted with the highest level of ethical standards in achieving its Vision and Mission.

### Risk Management

Specific steps taken by the Bank in managing both banking and non-banking risks are detailed on page 76 of this Report.

### Income

The Income of the Group for 2006 was Rs. 24,451.866 million (Rs. 16,225.377 million in 2005) while the Bank's income was Rs. 24,469.470 million (Rs. 16,099.645 million in 2005).

### Profit

The profits before tax of the Group and the Bank were up by 17.81% and 15.69% respectively (41.38% and 45.45% in 2005) and the profits after tax were down by 12.11% and 14.87% respectively (up by 36.53% and 40.33% in 2005).

The reasons for the decrease in the profit after tax are explained in the Financial Review section of the Management Discussion and Analysis on page 21.

Details of profit relating to the Bank are given below:

	2006 Rs.	2005 Rs.
Profit for the year after payment of all expenses of management and providing for depreciation, possible loan losses, Financial VAT and contingencies	4,213,546,068	3,641,960,619
Provision for taxation	2,200,917,452	1,277,720,676
Net profit after taxation	2,012,628,616	2,364,239,943
Transfer from Revaluation Reserve	-	256,279
Profit/(loss) brought forward from previous year	994,023	(1,785,630)
Profit available for appropriation	2,013,622,639	2,362,710,592
<b>Appropriations</b>		
Transfer to the Statutory Reserve Fund	7,500,000	412,000,000
Transfer to the Capital Redemption Reserve Fund	906,555,000	-
Transfer to General Reserve	187,500,000	1,080,000,000
<b>Dividends on Preference Shares</b>		
13% Cumulative Redeemable Preference Shares		
(Redeemed on Sep. 20, 2006)	84,918,124	117,852,150
11.25% Cumulative Redeemable Preference Shares		
	112,500,000	112,500,000
<b>Dividends on Ordinary Shares</b>		
15% Interim Dividend paid (15% in 2005)		
	214,128,939	213,121,473
<b>35% Final Dividend proposed (30% in 2005)</b>		
	499,865,534	426,242,946
Profit/(loss) to be carried forward	655,042	994,023

The dividend payout ratio (inclusive of the dividends on Preference Shares) amounts to 45.28% of the profit after tax of 2006, compared to 36.79% for 2005.

**Dividends on Ordinary Shares**

The Directors recommend the payment of 35% final dividend for the year 2006 (30% in 2005). An interim dividend of 15% was paid in November 2006 (15% in 2005).

Interim dividend was paid partly out of dividends received, which was not subject to further withholding tax. Final dividend will be paid partly out of dividends received and partly out of taxable profits of the Bank. The dividends paid out of profits will be exposed to withholding tax.

**Provision for Taxation**

Provision for taxation has been computed at the rates given in Note 9.1 to the Financial Statements.

**Corporate Donations**

During the year, the Bank made donations amounting to Rs. 13,505,145/- (Rs. 9,847,600/- in 2005) in terms of the resolution passed at the last Annual General Meeting. The donations made to Government approved charities from the above amounted to Rs. 3,432,000/- (Rs. 703,000/- in 2005).

**Property, Plant & Equipment**

Capital expenditure on Property, Plant & Equipment, Capital Work-in-Progress and Intangible Assets amounted to Rs. 574.828 million (Rs. 692.737 million in 2005), details of which are given in Note 23 and 24 to the Financial Statements. Capital expenditure approved and contracted for after the year end is given in Note 35 to the Financial Statements.

**Market Value of Freehold Properties**

All freehold land & buildings of the Bank were last revalued by professionally qualified independent valuers as at December 31, 2004, with the permission of the Central Bank of Sri Lanka. The Directors are of the opinion that the revalued amounts are not in excess of the current market values of such properties.

**Reserves**

The total reserves of the Group stood at Rs. 13,588.274 million as at December 31, 2006 (Rs. 12,626.209 million as at December 31, 2005) details of which are given in Notes 31 and 32 to the Financial Statements.

**Share Capital and Debentures**

The total issued and paid up ordinary share capital as at December 31, 2006 was Rs. 1,428.186 million consisting of 133,518,264 Ordinary Voting Shares of Rs. 10/- each and 9,300,460 Ordinary Non-Voting Shares of Rs.10/- each, compared to Rs. 1,420.809 million as at December 31, 2005. The increase in the share capital was due to 737,742 Ordinary Voting Shares being issued for a consideration of Rs. 60.063 million upon exercise of the options granted under the ESOP 2002 during the year.

In addition, the Company has Rs. 1,000.000 million worth 11.25% Cumulative Redeemable Preference Shares of Rs. 10/- each in issue. The funds raised therefrom have been used to expand the leasing and other long-term credit facilities.

The 13% five-year Cumulative Redeemable Preference Shares of the Bank which were allotted on September 21, 2001 amounting to Rs. 906.555 million, were redeemed on September 20, 2006. Since the Bank did not issue new shares for the redemption, an appropriation of profits equal to the nominal value of shares redeemed was made to the Capital Redemption Reserve Fund, in terms of Section 57 (1) (d) of the Companies Act No. 17 of 1982.

The details of share capital are given in Note 30 to the Financial Statements.

The Company has also raised Rs. 2,127.030 million through the issue of 2,127,030 Unsecured Subordinated Redeemable debentures of Rs. 1,000/- each, of which Rs. 1,000.000 million was issued during the year through a private placement. The funds raised from these debentures have been used to expand the leasing business and for other general corporate purposes.

The details of the debentures in issue as at December 31, 2006 are given in Note 29 to the Financial Statements.

**Share Information**

Information relating to earnings, dividends, net assets and market value per share is given in Financial Highlights on page 3 of this Report. Information on share trading is given on page 164 of this Report.

### Shareholdings

There were 6,213 registered shareholders (6,438 in 2005) holding Ordinary Voting Shares and 2,265 registered shareholders (2,410 in 2005) holding Ordinary Non-Voting Shares of the Bank as at December 31, 2006. The distribution of shareholding is given on page 162 of this Report.

### Equitable Treatment to Shareholders

Bank has made all endeavours to ensure equitable treatment to all shareholders.

### Directors

#### List of Directors

The Board of Directors of Commercial Bank of Ceylon Ltd. consists of 9 Directors with wide financial knowledge and experience. The qualifications and experience of the Directors are given on page 10 of this report.

The following were the Directors of the Bank as at the end of the year:

Mr. M.J.C. Amarasuriya (*Chairman*)  
 Mr. B.R.L. Fernando (*Deputy Chairman*)  
 Mr. A.L. Gooneratne (*Managing Director*)  
 Dr. H.S. Wanasinghe  
 Mr. A.N. Fonseka  
 Mr. L.J.A. Fernando  
 Mr. Iyad M. Malas  
 Mr. D.S. Weerakkody  
 Mr. G. Galludec (Alternate Director to Mr. Iyad M. Malas) (Appointed on July 14, 2006)  
 Deshamanya Ken Balendra (Appointed on October 2, 2006)

### Resignations, Appointments and Recommended Re-elections of Directors

#### Resignations

Mr. J.S. Mather (Resigned on March 16, 2006).  
 Mr. Sanjiva Senanayake (Resigned on July 14, 2006)

#### Appointments

Deshamanya Ken Balendra was appointed to the Board in terms of Article 92 of the Articles of Association of the Company on October 2, 2006, subject to the approval to be obtained from the Director of Bank Supervision of the Central Bank of Sri Lanka, which approval was obtained on October 16, 2006.

Mr. G. Galludec was appointed to the Board on July 14, 2006 as an Alternate Director to Mr. Iyad M. Malas in terms of the Article 74 of the Articles of Association of the Company, subject to the approval to be obtained from the Director of Bank supervision of the Central Bank of Sri Lanka, which approval was obtained on October 16, 2006.

### Recommended Re-elections

In accordance with Articles 85 & 86 of the Articles of Association of the Company, Mr. B.R.L. Fernando and Dr. H.S. Wanasinghe retire by rotation and being eligible for re-election are recommended for re-election.

Deshamanya Ken Balendra who was appointed to the Board to fill the casual vacancy which prevailed at the time of appointment, retires in terms of Article 92 of the Articles of Association of the Company and being eligible for re-election is recommended for re-election.

### Directors' Responsibility for Financial Reporting

The Directors are responsible for the preparation of Financial Statements of the Bank to reflect a true and fair view of the state of its affairs. The Directors are of the view that these Financial Statements have been prepared in conformity with the requirements of the Sri Lanka Accounting Standards, Companies Act No. 17 of 1982, the Banking Act No. 30 of 1988 and the Listing Rules of the Colombo Stock Exchange.

### Directors' Interests in Ordinary Shares

Shareholdings of the Directors at the beginning and at the end of the year were as follows:

	As at 31.12.06	As at 01.01.06
Mr. M.J.C. Amarasuriya	309,864	309,864
	104,932	104,932
	(non-voting)	(non-voting)
Mr. B.R.L. Fernando	4,778	4,778
	(non-voting)	(non-voting)
Mr. A.L. Gooneratne	390,158	390,158
	17,324	17,324
	(non-voting)	(non-voting)
Dr. H.S. Wanasinghe	-	-
Mr. A.N. Fonseka	622	622
	(non-voting)	(non-voting)
Mr. L.J.A. Fernando	-	-
Mr. Iyad M. Malas	-	-
Mr. G. Galludec	-	-
Mr. D.S. Weerakkody	-	-
Deshamanya Ken Balendra	-	-
Percentage shareholding of the Directors-		
Ordinary Voting Shares	0.52%	0.53%
Ordinary Non-Voting Shares	1.37%	1.37%

Directors' shareholdings have not changed subsequent from the date of the Balance Sheet up to January 15, 2007 being one month prior to the date of Notice of the Annual General Meeting.

**Directors' Interests in Cumulative Redeemable Preference Shares**

There were no Cumulative Redeemable Preference Shares registered in the names of the Directors as at the beginning and at the end of the year.

**Directors' Interests in Debentures**

There were no debentures registered in the names of the Directors as at the beginning and at the end of the year.

**Employee Share Ownership/Option Plans**

The details of the Employee Share Option Plan are given in Note 30 to the Financial Statements.

**Directors' Interests in Contracts**

Directors' interests in contracts or proposed contracts with the Company, both direct and indirect are disclosed in Note 37 to the Financial Statements. These interests have been declared at Directors' Meetings. Directors have refrained from voting on matters in which they were materially interested. Directors have no direct or indirect interest in any other contract or proposed contract with the Company.

**Compliance with Laws and Regulations**

The Bank/Group has not engaged in any activities contravening the laws and regulations. All those responsible for ensuring compliance with the provisions in various laws and regulations quarterly confirm their compliance to the Board Audit Committee.

**Environmental Protection**

The Bank/Group has not engaged in any activity, which is harmful to the environment. Specific measures taken to protect the environment are given in the Community Impact Report on page 73 of this Report.

**Statutory Payments**

The Directors, to the best of their knowledge and belief are satisfied that all statutory payments due to the Government and in relation to the employees have been made in time.

**Events after the Balance Sheet Date**

There have not been any material events that occurred subsequent to the date of the Balance Sheet that require adjustments to the Financial Statements, other than those disclosed, if any, in Note 40 to the Financial Statements.

**Going Concern**

The Board of Directors is satisfied that the Bank has adequate resources to continue its operations in the foreseeable future. Accordingly, the Financial Statements are prepared based on the going concern concept.

**Appointment of Auditors**

The retiring Auditors, Messrs. Ernst & Young have signified their willingness to continue in office and a resolution to reappoint them as Auditors and authorising the Directors to fix their remuneration will be proposed at the Annual General Meeting.

**Notice of Meeting**

Notice of Meeting relating to the Thirty-Eighth Annual General Meeting is given on page 178.

By Order of the Board,

  
**Mrs. R.R. Dunuwille**  
*Company Secretary*

February 15, 2007  
Colombo.

## Directors' Responsibility for Financial Reporting

Under Section 143 of the Companies Act No. 17 of 1982, Directors of the Company have responsibility for ensuring that the Company keeps proper books of account of all the transactions and prepares Financial Statements that give a true and fair view of the state of affairs and of the profit/loss for the year.

Accordingly, the Directors have caused the Bank to maintain proper books of account and review the financial reporting system at their regular meetings and through the Audit Committee. The Audit Committee Report is given on page 94 of this Report. The Financial Statements for the year 2006 prepared and presented in this Report are consistent with the underlying books of account and are in conformity with the requirements of the Companies Act, Sri Lanka Accounting Standards, the Banking Act No. 30 of 1988 and the Listing Rules of the Colombo Stock Exchange. The Directors consider that, in preparing the Financial Statements exhibited on pages 96 to 155 inclusive, they have adopted appropriate accounting policies on a consistent basis and supported by reasonable and prudent judgements and estimates.

The Directors also have taken such steps as are reasonably open to them to safeguard the assets of the Bank and to prevent and detect frauds and other

irregularities. In this regard, the Directors have instituted an effective and comprehensive system of internal controls comprising of internal check, internal audit and financial and other controls required to carry on the business of banking in an orderly manner, safeguard its assets and secure as far as practicable the accuracy and reliability of the records.

The Bank's Auditors, M/s. Ernst & Young, carry out reviews and sample checks on the system of internal controls as they consider appropriate and necessary for expressing their opinion on the Financial Statements.

M/s. Ernst & Young, the Auditors of the Bank have examined the Financial Statements made available by the Board of Directors together with all the financial records, related data, minutes of shareholders and Directors meetings and express their opinion which appears as reported by them on page 95 of this Report.

By Order of the Board,

  
**Mrs. R. R. Dunuwille**  
*Company Secretary*

February 15, 2007  
Colombo.

The Personnel and Remuneration Committee is headed by the Non-Executive Chairman and comprises of three other Non-Executive Directors and the Managing Director. The Managing Director who is responsible for the overall management of the Bank provides information to the Committee and participates in its deliberations. The Committee Members are nominated by the Board of Directors of the Bank.

The Committee determines the compensation and benefits of the members of the Corporate Management and establishes performance parameters in setting individual targets to the employees. The Bank's variable pay plan is determined according to the overall achievements of the Bank and pre-determined individual targets which are based on various performance parameters.

The level of bonuses payable on achievement of the targets is set at the level perceived as correct to provide the necessary incentives for Executives and Senior Managers. The Committee makes appropriate adjustments to the bonus payable in the event of over or under achievement of the Bank against those targets. In addition to the above, the Committee assesses and recommends to the Board on appointments to the Corporate Management and advise on their succession planning.

The Committee obtained the services of local and international companies to conduct salary surveys in order to benchmark the compensation package with the external market to ascertain the base pay and other benefits to make it attractive to the staff.

During the year, the Committee deliberated in detail on the proposals made by Hewitt Outsourcing Services (India) Ltd., a firm of consultants hired by the Bank for restructuring the Bank's Defined Benefit Pension Scheme to a Defined Contribution Pension Plan and recommended to the Board that it be adopted.

The Committee obtained the services of Hewitt Outsourcing Services (India) Ltd. to redesign the performance appraisal system of the Bank and the Variable Pay plan.

All the above activities of the Committee have helped the Bank in maintaining a market oriented remuneration policy for the Bank's staff enabling the Bank to attract the best personnel in the market while maintaining a contended staff.

**M.J.C. Amarasuriya**  
*Chairman*

February 15, 2007  
Colombo.

The Audit Committee comprises of three Non-Executive Directors of the Bank, with the Managing Director attending the Meetings by invitation. During the year the depth of the Committee was further enhanced with the engagement of a practicing Chartered Accountant as a Consultant to the Committee with the concurrence of the Board of Directors. The Bank's Deputy General Manager – Inspection, functioned as the Secretary of the Committee.

The Committee is empowered, amongst other things, to examine any matter relating to the financial and other connected affairs of the Bank, to review all internal and external audit and inspection programmes, internal control systems and procedures, accounting policies and the adherence to statutory and regulatory compliance requirements etc., thus ensuring that a sound financial reporting system, which is well managed in order to provide accurate, appropriate and timely information to the Board of Directors, Management, Regulatory Authorities and Shareholders is in place. The Audit Committee ensures that the Bank's policies and operations conform to rules, regulations and accepted ethical guidelines.

During the year under review, the Committee met four times and carried out the following tasks:

1. Examined over 210 Audit and Inspection Reports on Branches and Head Office Departments and followed up on operational deficiencies or shortcomings which had been observed. Members of the Committee also undertook visits to some of the Branches, in order to be better appraised of Branch operations.
2. Met with the External Auditors prior to the commencement and at the conclusion of the Annual Audit and reviewed the Auditors' Management Letter, together with the Management's response thereto. The annual financial statements were also reviewed with the External Auditors.
3. Regularly, monitored the effectiveness of the internal financial controls and the procedures established for identifying and effectively assessing and managing risks. The Corporate Management was invited to make Presentations on "Risk Management measures adopted in their areas of responsibility".

4. Revised the Charter of the Audit Committee and obtained Board concurrence for the amendments. The annual evaluation on the effectiveness of the Audit Committee was done by the other Members of the Board of Directors, who assessed the overall outcome as satisfactory. The Committee will address itself to the areas which require strengthening as highlighted by this assessment.
5. Reviewed quarterly the Bank's compliance with mandatory banking and other statutory requirements and bi-annually, the Bank's adherence to the risk management measures approved by the Board.
6. Reviewed major decisions taken by the "Assets and Liabilities Committee" and "Credit Policy and Portfolio Review Committee" of the Bank. All exceptional items charged to the Income Statement were scrutinised, Bank's Chart of Accounts were closely examined to clear long outstanding items while credit monitoring procedures were further strengthened.
7. With the concurrence of the Board, enlisted the services of five Firms of Chartered Accountants, approved by the Central Bank of Sri Lanka, to supplement the Bank's Inspection Department, in carrying out Branch inspections.

The proceedings of the Audit Committee Meetings are regularly reported to the Board of Directors.

The Committee is of the view that adequate controls and procedures are in place to provide reasonable assurance that the Bank's assets are safeguarded and that the financial position of the Bank is well monitored.

The Audit Committee has recommended to the Board of Directors that Messrs. Ernst & Young be re-appointed as Auditors for the financial year ending December 31, 2007 subject to the approval of the Shareholders at the next Annual General Meeting.

**B.R.L Fernando**  
*Chairman - Audit Committee*

February 19, 2007



■ Chartered Accountants

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**AUDITORS' REPORT TO THE MEMBERS OF COMMERCIAL BANK OF CEYLON LIMITED**

We have audited the balance sheet of Commercial Bank of Ceylon Limited ("Bank") as at December 31, 2006, the Consolidated Balance Sheet of the Bank and its subsidiaries as at that date and the related Statements of Income, Cash Flows and Changes in Equity for the year then ended, together with the Accounting Policies and Notes as set out on pages 101 to 155.

**Respective Responsibilities of Directors and Auditors**

The Directors are responsible for preparing and presenting these financial statements in accordance with the Sri Lanka Accounting Standards. Our responsibility is to express an opinion on these financial statements, based on our audit.

**Basis of Opinion**

We conducted our audit in accordance with the Sri Lanka Auditing Standards, which require that we plan and perform the audit to obtain reasonable assurance about whether the said financial statements are free of material misstatements. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the said financial statements, assessing the accounting principles used and significant estimates made by the directors, evaluating the overall presentation of the financial statements, and determining whether the said financial statements are prepared and presented in accordance with the Sri Lanka Accounting Standards. We have obtained all the information and explanations, which to the best of my knowledge and belief were necessary for the purpose of our audit. We therefore believe that our audit provides a reasonable basis for our opinion.

**Opinion**

In our opinion, so far as appears from our examinations, the Bank has maintained proper books of account for the year ended December 31, 2006, and to the best of our

information and according to the explanations given to us, the said Balance Sheet and related Statements of Income, Cash Flows and Changes in Equity and the Accounting Policies and Notes thereto, which are in agreement with the said books and have been prepared and presented in accordance with the Sri Lanka Accounting Standards, provide the information required by the Companies Act No.17 of 1982 and the Banking Act No. 30 of 1988 and amendments thereto and give a true and fair view of the Bank's state of affairs as at December 31, 2006 and its Profits and Cash Flows for the year then ended.

In our opinion, the Consolidated Balance Sheet and Statements of Income, Cash Flows and Changes in Equity and the Accounting Policies and Notes thereto have been properly prepared and presented in accordance with the Sri Lanka Accounting Standards, provides the information required by the Companies Act No. 17 of 1982 and the Banking Act No. 30 of 1988 and amendments thereto and give a true and fair view of the state of affairs as at December 31, 2006 and of its Profit and Cash Flows for the year then ended of the Bank and its subsidiaries dealt with thereby, so far as concerns the members of the Bank.

**Directors' Interest in Contracts with the Bank**

According to the information made available to us, the Directors of the Bank were not directly or indirectly interested in contracts with the Bank during the year ended December 31, 2006, except as stated in Note 37 to these financial statements.

**Ernst & Young**

Chartered Accountants

Colombo

February 15, 2007

■ Partners : A D B Talwate FCA FCMA T K Bandaranayake FCA M P D Cooray FCA FCMA  
Ms. Y A De Silva ACA W R H Fernando FCA FCMA A P A Gunasekera FCA FCMA  
A Herath FCA D K Hulangamuwa ACA FCMA LLB (Lond) A S M Ismail ACA FCMA  
H M A Jayasinghe FCA FCMA Ms. G G S Manatunga ACA Ms. L C G Nanayakkara FCA FCMA

## Income Statement

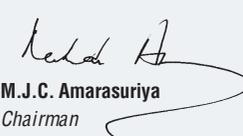
For the year ended December 31,	Bank			Group			
	Note	2006 Rs.'000	2005 Rs.'000	Change %	2006 Rs.'000	2005 Rs.'000	Change %
<b>Income</b>		<b>24,469,470</b>	16,099,645	51.99	<b>24,451,866</b>	16,225,377	50.70
Interest income	1	<b>19,531,748</b>	13,033,870	49.85	<b>19,537,228</b>	13,293,818	46.96
Less: Interest expenses	2	<b>11,954,610</b>	7,226,060	65.44	<b>11,944,666</b>	7,458,430	60.15
Net interest income		<b>7,577,138</b>	5,807,810	30.46	<b>7,592,562</b>	5,835,388	30.11
Foreign exchange profit		<b>1,439,008</b>	586,915	145.18	<b>1,439,008</b>	586,915	145.18
Fees and commission income	3	<b>2,011,285</b>	1,759,704	14.30	<b>2,011,191</b>	1,759,619	14.30
Other income	4	<b>1,487,429</b>	719,156	106.83	<b>1,464,439</b>	585,025	150.32
		<b>12,514,860</b>	8,873,585	41.03	<b>12,507,200</b>	8,766,947	42.66
Less: Operating expenses	5						
Personnel costs		<b>2,559,721</b>	2,128,177	20.28	<b>2,566,189</b>	2,143,859	19.70
Premises, equipment and establishment expenses		<b>1,402,434</b>	1,163,615	20.52	<b>1,384,099</b>	1,146,394	20.74
Provision for staff retirement benefits	6	<b>1,813,835</b>	235,971	668.67	<b>1,813,835</b>	235,971	668.67
Loan losses and provisions	7	<b>655,070</b>	414,864	57.90	<b>655,070</b>	414,864	57.90
Other overhead expenses		<b>1,870,255</b>	1,288,998	45.09	<b>1,829,308</b>	1,258,273	45.38
		<b>8,301,315</b>	5,231,625	58.68	<b>8,248,501</b>	5,199,361	58.64
Profit from operations		<b>4,213,545</b>	3,641,960	15.69	<b>4,258,699</b>	3,567,586	19.37
Add/(less): Share of profit/(loss) before tax of Associate Companies	8	<b>–</b>	–	–	<b>62,454</b>	100,462	(37.83)
<b>Profit before taxation</b>		<b>4,213,545</b>	3,641,960	15.69	<b>4,321,153</b>	3,668,048	17.81
Less: Provision for taxation	9	<b>2,200,917</b>	1,277,720	72.25	<b>2,248,751</b>	1,309,969	71.66
<b>Profit after taxation</b>		<b>2,012,628</b>	2,364,240	(14.87)	<b>2,072,402</b>	2,358,079	(12.11)
Attributable to:							
Equity holders of the parent		<b>2,012,628</b>	2,364,240	(14.87)	<b>2,070,707</b>	2,356,438	(12.13)
Minority interest		<b>–</b>	–	–	<b>1,695</b>	1,641	3.29
		<b>2,012,628</b>	2,364,240	(14.87)	<b>2,072,402</b>	2,358,079	(12.11)
Basic Earnings per Ordinary Share	10	<b>Rs. 12.71</b>	Rs. 14.94	(14.93)	<b>Rs. 13.12</b>	Rs. 14.89	(11.89)
Diluted Earnings per Ordinary Share	10	<b>Rs. 12.48</b>	Rs. 14.67	(14.93)	<b>Rs. 12.88</b>	Rs. 14.62	(11.90)
Dividend per Ordinary Share		<b>Rs. 5.00</b>	Rs. 4.50	11.11	<b>Rs. 5.00</b>	Rs. 4.50	11.11

The Accounting Policies and the Notes from pages 101 to 155 form an integral part of these Financial Statements.

As at December 31,	Note	Bank			Group		
		2006 Rs.'000	2005 Rs.'000	Change %	2006 Rs.'000	2005 Rs.'000	Change %
<b>ASSETS</b>							
Cash and short-term funds	13	13,738,709	18,662,853	(26.38)	13,731,439	18,656,759	(26.40)
Balances with Central Banks	14	12,573,651	9,045,180	39.01	12,573,651	9,045,180	39.01
Government Treasury Bills and Bonds	15	12,040,309	11,410,083	5.52	12,221,771	11,665,496	4.77
Commercial paper		422,783	407,567	3.73	422,783	407,567	3.73
Securities purchased under resale agreements		4,593,089	808,135	468.36	4,593,089	808,135	468.36
Dealing securities	16	144,896	182,243	(20.49)	144,896	182,243	(20.49)
Investments held for sale	17	218,392	-	-	401,259	-	-
Investments held to maturity	18	1,393,779	3,091,372	(54.91)	1,393,879	3,091,472	(54.91)
Treasury Bonds maturing after one year		20,024,893	9,808,477	104.16	20,024,893	9,808,477	104.16
Bills of Exchange	19.1	3,288,198	2,790,316	17.84	3,288,198	2,790,316	17.84
Loans & advances	19.2	137,725,861	108,884,242	26.49	137,720,172	108,883,886	26.48
Lease receivable within one year	19.3	3,035,428	2,484,227	22.19	3,006,608	2,460,247	22.21
Lease receivable from one to five years	19.4	6,465,175	4,596,246	40.66	6,397,494	4,536,924	41.01
Lease receivable after five years	19.5	17,377	7,996	117.32	17,377	7,996	117.32
		<b>215,682,540</b>	<b>172,178,937</b>	<b>25.27</b>	<b>215,937,509</b>	<b>172,344,698</b>	<b>25.29</b>
Investments in Associate Companies	20	44,331	107,081	(58.60)	40,965	282,789	(85.51)
Investments in Subsidiary Companies	21	433,681	433,681	-	-	-	-
Interest and fees receivable		1,638,893	1,183,626	38.46	1,638,893	1,198,631	36.73
Other assets	22	2,796,017	2,991,791	(6.54)	2,842,982	2,919,779	(2.63)
Property, Plant & Equipment	23	3,217,262	3,032,362	6.10	3,437,522	3,238,039	6.16
Intangible assets	24	161,529	149,985	7.70	162,768	151,115	7.71
<b>Total Assets</b>		<b>223,974,253</b>	<b>180,077,463</b>	<b>24.38</b>	<b>224,060,639</b>	<b>180,135,051</b>	<b>24.38</b>
<b>LIABILITIES</b>							
Deposits from customers	25	157,634,070	127,601,280	23.54	157,531,828	127,490,713	23.56
Dividends payable		112,500	230,352	(51.16)	112,500	230,352	(51.16)
Borrowings	26	18,944,116	13,387,062	41.51	18,944,116	13,387,062	41.51
Securities sold under repurchase agreements		14,330,006	11,389,174	25.82	14,317,063	11,386,147	25.74
Other liabilities	27	8,404,027	6,115,902	37.41	8,402,043	6,108,924	37.54
Tax payable		1,445,718	817,754	76.79	1,420,226	784,218	81.10
Deferred taxation	28	580,535	214,146	171.09	624,940	227,367	174.86
Debentures	29	6,680,440	4,553,410	46.71	6,680,440	4,553,410	46.71
<b>Total Liabilities</b>		<b>208,131,412</b>	<b>164,309,080</b>	<b>26.67</b>	<b>208,033,156</b>	<b>164,168,193</b>	<b>26.72</b>
<b>SHAREHOLDERS' FUNDS</b>							
Share capital	30	2,428,186	3,327,364	(27.02)	2,428,186	3,327,364	(27.02)
Statutory Reserve Fund	31	1,428,500	1,421,000	0.53	1,429,319	1,421,819	0.53
Reserves	32	11,986,155	11,020,019	8.77	12,158,955	11,204,390	8.52
Shareholders' funds		<b>15,842,841</b>	<b>15,768,383</b>	<b>0.47</b>	<b>16,016,460</b>	<b>15,953,573</b>	<b>0.39</b>
Minority Interest		-	-	-	11,023	13,285	(17.03)
<b>Total shareholders' funds and minority interest</b>		<b>15,842,841</b>	<b>15,768,383</b>	<b>0.47</b>	<b>16,027,483</b>	<b>15,966,858</b>	<b>0.38</b>
<b>Total liabilities, shareholders' funds and minority interest</b>		<b>223,974,253</b>	<b>180,077,463</b>	<b>24.38</b>	<b>224,060,639</b>	<b>180,135,051</b>	<b>24.38</b>
<b>Commitments and contingencies</b>	34	<b>53,623,918</b>	<b>47,153,953</b>	<b>13.72</b>	<b>53,623,918</b>	<b>47,153,953</b>	<b>13.72</b>
Net assets value per ordinary share		<b>Rs. 103.93</b>	<b>Rs. 97.06</b>	<b>7.08</b>	<b>Rs. 105.14</b>	<b>Rs. 98.36</b>	<b>6.89</b>

The Accounting Policies and the Notes from pages 101 to 155 form an integral part of these Financial Statements.

Approved and signed for and on behalf of the Board

  
**M.J.C. Amarasuriya**  
 Chairman  
 February 15, 2007  
 Colombo

  
**B.R.L. Fernando**  
 Deputy Chairman

  
**A.L. Gooneratne**  
 Managing Director

  
**Mrs. R.R. Dunuwille**  
 Company Secretary

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## Statement of Changes in Equity

For the year ended December 31, 2006

	Note	Share Capital			Statutory Reserve Fund	Reserves						Total Shareholders' Funds	Minority Interest	Total Equity
		Ordinary Voting Shares	Ordinary Non-Voting Shares	Cum. Red. Preference Shares		Capital Redemption Reserve	Share Premium	Revaluation Reserve	General Reserve	Foreign Currency Translation Reserve	Unappropriated Profit/(Loss) carried forward			
		Rs. '000	Rs. '000	Rs. '000	Rs. '000	Rs. '000	Rs. '000	Rs. '000	Rs. '000	Rs. '000	Rs. '000	Rs. '000	Rs. '000	Rs. '000
<b>BANK</b>														
Balance as at 31.12.2004		650,298	46,501	1,906,555	1,009,000	-	2,186,874	1,288,433	6,545,000	-	278,856	13,911,517	-	13,911,517
Final dividend for 2004		-	-	-	-	-	-	-	-	-	(280,641)	(280,641)	-	(280,641)
Issue of Ordinary Shares under Employee Share Option Plan		13,616	-	-	-	-	203,124	-	-	-	-	216,740	-	216,740
Bonus issue of Ordinary Shares		663,892	46,502	-	-	-	(710,394)	-	-	-	-	-	-	-
Reversal of Surplus on revaluation of property		-	-	-	-	-	-	(256)	-	-	256	-	-	-
Net profit for the year 2005		-	-	-	-	-	-	-	-	-	2,364,240	2,364,240	-	2,364,240
Transfers to Statutory Reserve Fund during the year 2005		-	-	-	412,000	-	-	-	-	-	(412,000)	-	-	-
Transfers during the year 2005		-	-	-	-	-	-	1,080,000	-	-	(1,080,000)	-	-	-
Dividends for 2005	11	-	-	-	-	-	-	-	-	-	(443,473)	(443,473)	-	(443,473)
Balance as at 31.12.2005		1,327,806	93,003	1,906,555	1,421,000	-	1,679,604	1,288,177	7,625,000	-	427,238	15,768,383	-	15,768,383
Final dividend for 2005		-	-	-	-	-	-	-	-	-	(426,243)	(426,243)	-	(426,243)
Issue of Ordinary Shares under Employee Share Option Plan		7,377	-	-	-	-	52,686	-	-	-	-	60,063	-	60,063
Debenture issue expenses written-off		-	-	-	-	-	(3,497)	-	-	-	-	(3,497)	-	(3,497)
Changes in accounting policy		-	-	-	-	-	-	-	404,375	(404,375)	-	-	-	-
Prior year adjustment for Deferred Tax on Leased Assets		-	-	-	-	-	-	-	(357,113)	-	-	(357,113)	-	(357,113)
Appreciation in the value of investment in Comtrust Equity Fund		-	-	-	-	-	-	-	118,396	-	-	118,396	-	118,396
Net unrealised gains/(losses) from Bangladesh translation		-	-	-	-	-	-	-	-	(11,674)	-	(11,674)	-	(11,674)
Net profit for the year 2006		-	-	-	-	-	-	-	-	-	2,012,628	2,012,628	-	2,012,628
Redemption of Preference shares		-	-	(906,555)	-	-	-	-	-	-	-	(906,555)	-	(906,555)
Transfer to CRRF Account		-	-	-	-	906,555	-	-	-	-	(906,555)	-	-	-
Transfers to Statutory Reserve Fund during the year 2006		-	-	-	7,500	-	-	-	-	-	(7,500)	-	-	-
Transfers during the year 2006		-	-	-	-	-	-	-	187,500	-	(187,500)	-	-	-
Dividends for 2006	11	-	-	-	-	-	-	-	-	-	(411,547)	(411,547)	-	(411,547)
Balance as at 31.12.2006		1,335,183	93,003	1,000,000	1,428,500	906,555	1,728,793	1,288,177	7,978,158	(416,049)	500,521	15,842,841	-	15,842,841
<b>GROUP</b>														
Balance as at 31.12.2004		650,298	46,501	1,906,555	1,009,819	-	2,186,874	1,288,433	6,545,000	-	471,029	14,104,509	12,364	14,116,873
Final dividend for 2004		-	-	-	-	-	-	-	-	-	(280,641)	(280,641)	-	(280,641)
Issue of Ordinary Shares under Employee Share Option Plan		13,616	-	-	-	-	203,124	-	-	-	-	216,740	-	216,740
Bonus issue of Ordinary Shares		663,892	46,502	-	-	-	(710,394)	-	-	-	-	-	-	-
Reversal of Surplus on revaluation of property		-	-	-	-	-	-	(256)	-	-	256	-	-	-
Net profit for the year 2005		-	-	-	-	-	-	-	-	-	2,356,438	2,356,438	1,641	2,358,079
Transfers to Statutory Reserve Fund during the year 2005		-	-	-	412,000	-	-	-	-	-	(412,000)	-	-	-
Transfers during the year 2005		-	-	-	-	-	-	1,080,000	-	-	(1,080,000)	-	-	-
Dividends for 2005	11	-	-	-	-	-	-	-	-	-	(443,473)	(443,473)	(720)	(444,193)
Balance as at 31.12.2005		1,327,806	93,003	1,906,555	1,421,819	-	1,679,604	1,288,177	7,625,000	-	611,609	15,953,573	13,285	15,966,858
Final dividend for 2005		-	-	-	-	-	-	-	-	-	(426,243)	(426,243)	-	(426,243)
Issue of Ordinary Shares under Employee Share Option Plan		7,377	-	-	-	-	52,686	-	-	-	-	60,063	-	60,063
Debenture issue expenses written-off		-	-	-	-	-	(3,497)	-	-	-	-	(3,497)	-	(3,497)
Changes in accounting policy		-	-	-	-	-	-	-	404,375	(404,375)	-	-	-	-
Changes in accounting policy on accounting for deferred taxation of Associate Companies		-	-	-	-	-	-	-	-	-	(41,838)	(41,838)	-	(41,838)
Prior year adjustment for Deferred Tax on Leased Assets		-	-	-	-	-	-	-	(357,113)	-	-	(357,113)	-	(357,113)
Prior year adjustment for Deferred Tax on classification of Retained Earnings		-	-	-	-	-	-	-	-	-	(27,812)	(27,812)	(1,603)	(29,415)
Appreciation in the value of investment in Comtrust Equity Fund		-	-	-	-	-	-	-	118,396	-	-	118,396	-	118,396
Net unrealised gains/(losses) from Bangladesh translation		-	-	-	-	-	-	-	-	(11,674)	-	(11,674)	-	(11,674)
Net profit for the year 2006		-	-	-	-	-	-	-	-	-	2,070,707	2,070,707	1,695	2,072,402
Redemption of Preference shares		-	-	(906,555)	-	-	-	-	-	-	-	(906,555)	-	(906,555)
Transfer to CRRF Account		-	-	-	-	906,555	-	-	-	-	(906,555)	-	-	-
Transfers to Statutory Reserve Fund during the year 2006		-	-	-	7,500	-	-	-	-	-	(7,500)	-	-	-
Transfers during the year 2006		-	-	-	-	-	-	-	187,500	-	(187,500)	-	-	-
Dividends for 2006	11	-	-	-	-	-	-	-	-	-	(411,547)	(411,547)	(2,354)	(413,901)
Balance as at 31.12.2006		1,335,183	93,003	1,000,000	1,429,319	906,555	1,728,793	1,288,177	7,978,158	(416,049)	673,321	16,016,460	11,023	16,027,483

Composition of the unappropriated profit/(loss) carried forward is given in Note 12 to the Financial Statements.

<i>For the year ended December 31,</i>	<b>Bank</b>		<b>Group</b>	
	<b>2006</b> Rs.'000	2005 Rs.'000	<b>2006</b> Rs.'000	2005 Rs.'000
<b>Cash Flows from Operating Activities</b>				
Interest and commission receipts	<b>21,072,011</b>	14,695,968	<b>21,090,452</b>	14,984,017
Interest payments	<b>(11,392,443)</b>	(6,880,871)	<b>(11,382,499)</b>	(7,113,241)
Recoveries on loans previously provided/written-off	<b>252,493</b>	198,949	<b>252,493</b>	198,949
Foreign exchange profit and other receipts	<b>1,557,176</b>	611,888	<b>1,567,779</b>	631,230
Cash payments to employees and suppliers	<b>(7,270,466)</b>	(4,517,594)	<b>(7,183,818)</b>	(4,455,629)
Operating profit before changes in operating assets	<b>4,218,771</b>	4,108,340	<b>4,344,407</b>	4,245,326
(Increase)/Decrease in operating assets:				
Balances with Central Banks	<b>(3,528,471)</b>	(2,725,500)	<b>(3,528,471)</b>	(2,725,500)
Funds advanced to customers	<b>(32,424,082)</b>	(28,240,979)	<b>(32,405,550)</b>	(28,227,823)
Increase/(Decrease) in operating liabilities:				
Deposits from customers	<b>30,028,253</b>	28,892,082	<b>30,036,578</b>	28,889,841
Negotiable certificates of deposit	<b>4,537</b>	(20,643)	<b>4,537</b>	(20,643)
Net cash from operating activities before income tax	<b>(1,700,992)</b>	2,013,300	<b>(1,548,499)</b>	2,161,201
Income tax paid	<b>(1,547,922)</b>	(968,106)	<b>(1,567,382)</b>	(996,455)
<b>Net cash inflow/(outflow) from operating activities</b>	<b>(3,248,914)</b>	1,045,194	<b>(3,115,881)</b>	1,164,746
<b>Cash Flows from Investing Activities</b>				
Dividends received	<b>96,663</b>	185,342	<b>49,223</b>	54,480
Interest received	<b>65,341</b>	158,570	<b>65,341</b>	158,570
Government Treasury Bills and Bonds	<b>(625,496)</b>	(13,422,381)	<b>(551,545)</b>	(12,577,749)
Securities purchased under resale agreements	<b>(3,784,954)</b>	(408,983)	<b>(3,784,954)</b>	1,279,285
Securities sold under repurchase agreements	<b>2,940,832</b>	2,339,281	<b>2,930,916</b>	(875,305)
Commercial paper	<b>(15,216)</b>	152,122	<b>(15,216)</b>	152,122
Treasury Bonds maturing after one year	<b>(10,216,416)</b>	12,064,094	<b>(10,216,416)</b>	12,664,810
Disposal/(Additions) of Dealing Securities	<b>37,347</b>	(72,683)	<b>37,347</b>	(72,683)
Additions to investments	<b>(856,298)</b>	(1,381,119)	<b>(856,298)</b>	(1,376,831)
Income from Associate Companies	–	–	<b>11,385</b>	24,534
Proceeds from matured investments	<b>1,514,147</b>	722,545	<b>1,514,147</b>	722,545
Proceeds from sale of investments held to maturity	<b>1,948,661</b>	64,713	<b>1,948,661</b>	64,713
Purchase of Property, Plant & Equipment	<b>(574,828)</b>	(692,737)	<b>(625,112)</b>	(730,564)
Proceeds from sale of Property, Plant & Equipment	<b>6,476</b>	54,005	<b>12,526</b>	57,691
<b>Net cash inflow/(outflow) from investing activities</b>	<b>(9,463,741)</b>	(237,231)	<b>(9,479,995)</b>	(454,382)
<b>Cash Flows from Financing Activities</b>				
Dividends paid to Minority Shareholders	–	–	<b>(3,957)</b>	(720)
Proceeds from issue of shares	<b>60,063</b>	–	<b>60,063</b>	–
Proceeds from issue of Debentures	<b>2,127,030</b>	1,309,000	<b>2,127,030</b>	1,309,000
Redemption of preference shares	<b>(906,555)</b>	–	<b>(906,555)</b>	–
Debenture issue expenses incurred	<b>(3,497)</b>	–	<b>(3,497)</b>	–
Net increase in other borrowings	<b>7,467,112</b>	5,134,397	<b>7,353,114</b>	5,228,481
Dividends paid	<b>(955,642)</b>	(724,114)	<b>(955,642)</b>	(726,082)
<b>Net cash inflow/(outflow) from financing activities</b>	<b>7,788,511</b>	5,719,283	<b>7,670,556</b>	5,810,679

## Cash Flow Statement

<i>For the year ended December 31,</i>	<b>Bank</b>		<b>Group</b>	
	<b>2006</b>	2005	<b>2006</b>	2005
	<b>Rs.'000</b>	Rs.'000	<b>Rs.'000</b>	Rs.'000
<b>Net increase in cash and cash equivalents</b>	<b>(4,924,144)</b>	6,527,246	<b>(4,925,320)</b>	6,521,043
<b>Cash and cash equivalents at beginning of the period</b>	<b>18,662,853</b>	12,135,607	<b>18,656,759</b>	12,135,716
<b>Cash and cash equivalents at end of the period (Refer to Note 13)</b>	<b>13,738,709</b>	18,662,853	<b>13,731,439</b>	18,656,759
<b>Reconciliation of Operating Profit</b>				
Profit before taxation	<b>4,213,545</b>	3,641,960	<b>4,321,153</b>	3,668,048
Add/(Less):				
Accrued Interest on loans and advances	<b>(455,267)</b>	(86,511)	<b>(440,262)</b>	(55,315)
Accrued Interest on deposits and borrowings	<b>562,167</b>	345,189	<b>562,167</b>	345,189
Investment income	<b>(305,498)</b>	(440,672)	<b>(269,443)</b>	(334,344)
Share of (profit)/loss of Associate Companies	-	-	<b>(62,454)</b>	(100,462)
Notional tax credit on interest on Treasury Bills and Bonds	<b>(15,755)</b>	(11,095)	<b>(17,705)</b>	(14,105)
(Profit)/Loss on sale of shares	<b>(802,669)</b>	(63,213)	<b>(802,669)</b>	(63,213)
(Profit)/Loss on sale of Property, Plant & Equipment	<b>(3,871)</b>	(31,008)	<b>(8,163)</b>	(33,323)
Depreciation	<b>375,779</b>	299,167	<b>409,613</b>	328,868
Loan losses & provisions	<b>655,070</b>	414,864	<b>655,070</b>	414,864
(Gain)/Loss on Mark to Market Valuation	<b>(4,730)</b>	39,659	<b>(4,730)</b>	64,585
Dividends received from Associate Companies	-	-	<b>1,830</b>	24,534
Operating profit before changes in operating assets	<b>4,218,771</b>	4,108,340	<b>4,344,407</b>	4,245,326

### 1. General

Commercial Bank is a public quoted company incorporated on June 25, 1969 and domiciled in Sri Lanka. Its registered office is at 'Commercial House', No. 21, Bristol Street, Colombo 1. The shares of the Bank have a primary listing on the Colombo Stock Exchange.

The Consolidated Financial Statements of the Bank for the year ended December 31, 2006 comprise the Bank (parent company) and its subsidiaries (together referred to as the "Group") and the Group's interest in its associate companies.

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

The Financial Statements for the year ended December 31, 2006 were authorised for issue on February 15, 2007, in accordance with a resolution of the Directors passed on February 15, 2007.

#### 1.1 Principal Activities

##### *Bank*

The principal activities of the Bank are banking and related activities such as accepting deposits, personal banking, trade financing, off-shore banking, resident and non-resident foreign currency operations, travel related services, corporate and retail credit, project financing, lease financing, rural credit, issuing of local and international credit cards, issuing of debit cards, telebanking facilities, bancassurance, internet banking, money remittance facilities, dealing in Government securities, bullion trading, export and domestic factoring, etc.

##### *Subsidiaries*

The principal activities of the Bank's subsidiaries, namely, Commercial Development Co. Ltd., ONEzero Company Ltd. and X-pertise Ltd. are property development, providing IT related services and training and development of human resource, respectively. Commercial Bank Primary Dealer Ltd., whose principal business activity was dealing in Government securities as a Primary Dealer, ceased its operations as at September 30, 2005, consequent to the Bank obtaining the licence to operate as a Primary Dealer. The proceedings for voluntary winding up of the Company are in progress.

##### *Associates*

The principal activities of the Bank's associates, namely, Commercial Leasing Company Ltd., Equity Investments Lanka Ltd. and Commercial Fund Management (Pvt) Ltd. are leasing and factoring, providing venture capital and fund management, respectively. The investments held by the Bank in both Commercial Leasing Company Ltd. and Commercial Fund Management (Pvt) Ltd. were classified as investments held for sale in accordance with the requirements of the Sri Lanka Accounting Standard No. 38 on Non-Current Assets Held for Sale and Discontinued Operations, with effect from June 30, 2006 and December 31, 2006 respectively, due to the Bank's decision to dispose its interests in these Associates.

#### 1.2 Basis of Preparation

The Financial Statements of the Bank are prepared under the historical cost convention, except that certain Government treasury bills and bonds, dealing securities, investments held for sale, investments held to maturity, treasury bonds maturing after one year and land and buildings are stated at valuation as explained in Notes 15, 16, 17, 18, and 23 to the Financial Statements. Assets and liabilities are grouped by nature and listed in an order that reflects their relative liquidity. These Financial Statements are prepared in Sri Lankan Rupees unless otherwise stated. Where appropriate the Significant Accounting Policies are disclosed in the succeeding notes.

#### 1.3 Statement of Compliance

The Consolidated Financial Statements of the Bank are prepared in accordance with the Sri Lanka Accounting Standards.

### 1.4 Basis of Consolidation

The Bank's Financial Statements comprise the amalgamation of the Financial Statements of the Domestic Banking Unit, the Off-Shore Banking Centre and the foreign operations of the Bank. The Group Financial Statements comprise consolidation of the Financial Statements of the Bank, its subsidiaries in terms of the Sri Lanka Accounting Standard No. 26 on Consolidated and separate Financial Statements and the proportionate share of the profit/loss of its associate companies in terms of the Sri Lanka Accounting Standard No. 27 on Investments in Associates.

#### 1.4.1 Subsidiaries

Subsidiaries are those entities controlled by the Bank. Subsidiaries are fully consolidated from the date on which control is transferred to the Bank. Control is achieved where the Bank has the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities. The results of subsidiaries acquired or disposed of during the year are included in the Consolidated Income Statement from the date of acquisition or up to the date of disposal, as appropriate. The Consolidated Financial Statements are prepared to a common financial year ending December 31. All Subsidiaries in the Group have a common financial year ending December 31.

A listing of the Group's subsidiaries is set out in Note No. 21 to the Financial Statements.

Minority interests represent the portion of profit or loss and net assets not owned, directly or indirectly, by the Bank and are presented separately in the Consolidated Income Statement and within equity in the Consolidated Balance Sheet, separately from parent shareholders' equity.

#### 1.4.2 Associates

The Bank's investments in its associates are accounted for in the Consolidated Financial Statements using the Equity Method of Accounting. An associate is an entity in which the Bank has significant influence and which is neither a subsidiary nor a joint venture.

Under the equity method, the investments in the associates are carried in the Balance Sheet at cost plus post-acquisition changes in the Bank's share of net assets of the associates. Losses in excess of the cost of the investment in an associate are recognised when the Bank has incurred obligations on its behalf. Goodwill relating to an associate is included in the carrying amount of the investment and is not amortised. The Income Statement reflects the Bank's share of the results of operations of the associate. Where there has been a change recognised directly in the equity of the associate, the Bank recognises its share of any changes and discloses this, when applicable, in the Statement of Changes in Equity. Profits and losses resulting from transactions between the Bank and the associates are eliminated to the extent of the interest in the associate.

The reporting dates of the associates and the Bank are identical and the associate's accounting policies largely conform to those used by the Bank for like transactions and events in similar circumstances.

A listing of the associate companies are set out in Note No. 20 to the Financial Statements.

#### 1.4.3 Business Combinations and Goodwill

Business combinations are accounted for using the Purchase Method of Accounting as per the requirements of Sri Lanka Accounting Standard No. 25 on Business Combinations. This involves recognising identifiable assets (including previously unrecognised intangibles) and liabilities (including contingent liabilities) of the acquired business at fair value. Any excess of the cost of acquisition over the fair values of the identifiable net assets acquired is recognised as goodwill. If the cost of acquisition is less than the fair values of the identifiable net assets acquired, the discount on acquisition is recognised directly in the Income Statement in the year of acquisition.

Goodwill acquired in a business combination is initially measured at cost, being the excess of the cost of the business combination over the Bank's interests in the net fair value of the identifiable assets, liabilities and contingent liabilities acquired. Sri Lanka Accounting Standard No. 25 on Business Combinations requires that following initial recognition goodwill to be measured at cost less any accumulated impairment losses and goodwill to be reviewed for impairment annually or more frequently if events or changes in circumstances indicate that the carrying value may be impaired.

However, acquired goodwill is written off in full in the year of acquisition, since the Bank is not permitted to pay dividends otherwise, as per the Section 22 of the Banking Act No. 30 of 1988.

When subsidiaries/associates/other business units are sold, the difference between the selling price and the net assets plus cumulative translation differences and unimpaired goodwill is recognised in the Income Statement.

No goodwill/discount on acquisition arose from the treatment of Associates under the Equity Method since Commercial Bank had the respective percentages of ownership in associates from the commencement of those associates.

#### **1.4.4 Transactions Eliminated on Consolidation**

All intra-group transactions and balances, income and expenses and any unrealised gains arising from such inter-company transactions and balances have been eliminated in full in preparing the Consolidated Financial Statements. Unrealised gains resulting from transactions with Associates are eliminated to the extent of the Group's interest in the associates. Unrealised losses are eliminated in the same way as unrealised gains unless there is evidence of impairment in value.

### **1.5 Changes in Accounting Policies**

The accounting policies adopted are consistent with those used in the previous financial year except as follows:

The Company has adopted the following new Sri Lanka Accounting Standards during the year

- SLAS 3 (revised) - Presentation of Financial Statements
- SLAS 10 (revised) - Accounting Policies, Changes in Accounting Estimates
- SLAS 12 (revised) - Events after the Balance Sheet Date
- SLAS 14 (revised) - Income Taxes
- SLAS 18 (revised) - Property, Plant & Equipment
- SLAS 19 (revised) - Leases
- SLAS 21 (revised) - The Effects of Changes in Foreign Exchange Rates
- SLAS 26 (revised) - Consolidated and Separate Financial Statements
- SLAS 27 (revised) - Accounting for Investments in Associates
- SLAS 30 (revised) - Related Party Disclosures
- SLAS 34 (revised) - Earnings per Share
- SLAS 38 (revised) - Non-current Assets held for Sale and Discontinued Operations
- SLAS 40 (revised) - Investments Property
- SLAS 41 (revised) - Impairments of Assets

## Significant Accounting Policies

The principal effect of these changes are as follows:

As of January 1, 2006, the Bank adopted the amendments to Sri Lanka Accounting Standard No. 3 on Presentation of Financial Statements under which share of profit and the share of net assets attributable to minority interest have been disclosed separately on the face of the Income Statement and in the Balance Sheet under the shareholders' funds. The effect of this change as at December 31, 2006 and December 31, 2005 has been incorporated in the Consolidated Financial Statements.

As of January 1, 2006, the Bank adopted the amendments to Sri Lanka Accounting Standard No. 14 on Income Taxes under which deferred tax is calculated on all temporary differences. Thus, deferred tax on assets leased to customers was provided. The effect of this change as at December 31, 2006 and December 31, 2005 has been incorporated in the Financial Statements.

As of January 1, 2006, the Bank adopted the amendments to Sri Lanka Accounting Standard No. 19 on Leases, under which leasehold lands which were hitherto classified under Property, Plant & Equipment was reclassified as prepayments and was accounted as part of other assets of the Bank.

As of January 1, 2006, the Bank adopted the amendments to Sri Lanka Accounting Standard No. 21 on the Effects of Changes in Foreign Exchange Rates. As a result, all exchange differences arising from monetary items that form part of the Bank's net investment in a foreign operation are recognised as a separate component of equity in the Consolidated Financial Statements regardless of the currency in which the monetary items are denominated. The effect of this change as at December 31, 2006 and December 31, 2005 has been incorporated in the Financial Statements.

As of January 1, 2006, the Bank adopted the Sri Lanka Accounting Standard No. 38 on Non-Current Assets Held for Sale and Discontinued Operations. Accordingly, investments in two associates namely Commercial Leasing Company Ltd. and Commercial Fund Management (Pvt.) Ltd., were classified under Investments held for sale as the Bank's Board decided to dispose these investments. In addition, a part of the investment made in the units of Comtrust Equity Fund too was classified under Investments held for sale as the Bank's Board decided to dispose this investment. The effect of this change as at December 31, 2006 and December 31, 2005 has been incorporated in the Financial Statements.

As of January 1, 2006, the Group adopted the Sri Lanka Accounting Standard No. 40 on Investment Property. Accordingly, leasehold buildings of Commercial Development Company Ltd., a subsidiary of the Bank were classified under Investment Property in the Financial Statements of that Company. However, in the Consolidated Financial Statements, the above leasehold buildings were accounted for under Property, Plant & Equipment as this property is considered as owner-occupied from the perspective of the Group as per the Sri Lanka Accounting Standard No. 40.

### 1.6 Foreign Currency Translation

The Consolidated Financial Statements are presented in Sri Lankan Rupees, which is the Bank's functional and presentation currency. Each entity in the group determines its own functional currency and items included in the Financial Statements of each entity are measured using that functional currency.

**1.6.1 Transactions and Balances**

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

Monetary assets and liabilities denominated in foreign currencies are re-translated at the middle exchange rate of the functional currency ruling at the Balance Sheet date. All differences are taken to Income Statement.

Non-monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rates as at the dates of the initial transactions. Non-monetary items measured at fair value in a foreign currency are translated using the exchange rates at the date when the fair value was determined. Any goodwill arising on the acquisition of a foreign operation and any fair value adjustments to the carrying amounts of assets and liabilities arising on the acquisition are treated as assets and liabilities of the foreign operations and translated at the closing rate.

**1.6.2** Forward exchange contracts are valued at the forward market rates ruling on the date of the Balance Sheet. Unrealised gains and losses are dealt with through the Income Statement.

**1.6.3** Transactions of the Off-Shore Banking Centre have been recorded in accordance with the paragraph 1.6.1 above except for the application of the year end exchange rate for the Income Statement.

**1.6.4** As at the Balance Sheet date, the assets and liabilities of the overseas branch operations are translated into the presentation currency of the Bank as at the rate of exchange ruling at the Balance Sheet date and their Income Statement is translated at the weighted average exchange rate for the year. The exchange differences arising on the translation are taken directly to a separate component of equity. On disposal of a foreign operation, the deferred cumulative amount recognised in equity relating to that particular foreign operation is recognised in the Income Statement.

**1.7 Taxation**

**1.7.1 Current Taxation**

Current tax assets and liabilities consist of amounts expected to be recovered from or paid to the taxation authorities in respect of the current as well as prior years. The tax rates and tax laws used to compute the amount are those that are enacted or substantially enacted by the Balance Sheet date. Accordingly, provision for taxation is made on the basis of the profit for the year as adjusted for taxation purposes in accordance with the provisions of the Inland Revenue Act No. 38 of 2000 and the amendments thereto, at the rates specified in Note No. 9.1 to the Financial Statements. Provision for taxation on the overseas branches is made on the basis of the profit for the year as adjusted for taxation purposes in accordance with the provisions of the relevant statutes in those countries.

**1.7.2 Deferred Taxation**

Deferred tax is provided on temporary differences at the Balance Sheet date between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes. Deferred tax liabilities are recognised for all temporary differences, except:

- Where the deferred tax liability arises from the initial recognition of goodwill or of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profits nor taxable profits or loss; and
- In respect of taxable temporary differences associated with investments in subsidiaries and associates, where the timing of the reversal of the temporary differences can be controlled and it is probable that the temporary differences will not reverse in the foreseeable future.

## Significant Accounting Policies

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

- Where the deferred tax assets relating to the deductible temporary difference arises from the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor the taxable profit or loss; and
- In respect of deductible temporary differences associated with investments in subsidiaries and associates, deferred tax assets are recognised only to the extent that it is probable that the temporary differences will reverse in the foreseeable future and taxable profits will be available against which the temporary differences can be utilised.

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

Deferred tax assets and liabilities are measured at the tax rates that are expected to apply in the year when the assets are realised, or the liabilities are settled, based on tax rates and tax laws that have been enacted or substantially enacted at the Balance Sheet date.

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

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

### 1.8 Comparative Figures

Amounts shown for the previous year in respect of Interest income, Other income, Government Treasury Bills and Bonds, Investments held to maturity, Treasury Bonds maturing after one year, Loans and advances, Lease receivables within one year, Lease receivable from one to five years, Lease receivable after five years, Other assets, Property, Plant & Equipment, Borrowings, Other liabilities, Tax payable and Deferred taxation have been reclassified to facilitate comparison, in accordance with substance of the transaction.

### 1.9 Events after the Balance Sheet Date

All the material events after the Balance Sheet date have been considered and appropriate adjustments/disclosures have been made in Note No. 40 to the Financial Statements, where necessary.

## 2. Assets and Bases of their Valuation

### 2.1 Advances to Customers

Advances to customers are stated in the Balance Sheet net of provisions for possible loan losses and net of interest, which is not accrued to revenue.

**2.1.1 Provision for Loan Losses**

Specific provisions for possible loan losses are based on a continuous review of the loans and advances portfolio in accordance with the Sri Lanka Accounting Standard No. 23 on Revenue Recognition and Disclosures in the Financial Statements of Banks and the parameters set by the Central Bank of Sri Lanka. Accordingly, specific provisions have been made as follows:

<b>Period Outstanding</b>	<b>Classification</b>	<b>Minimum Provision made net of realisable Value of Security</b>
6 to 12 months	Sub-Standard	20%
12 to 18 months	Doubtful	50%
18 months and over	Loss	100%

Where necessary, provisions have been made over and above the minimum percentages on a case by case basis.

In addition, a general provision is made at the rate of 0.1% per quarter on performing and overdue loans and advances portfolio commencing the fourth quarter 2006, as per a direction from the Central Bank of Sri Lanka, which requires that a general provision up to 1% on total performing and overdue loans and advances portfolio be made on or before the end of the first quarter 2009.

**2.2 Foreclosed Properties**

Foreclosed properties are acquired in full or partial satisfaction of debts, are accounted for at the lower of cost or market value on an individual property basis. The shortfall between the prevailing market value of the foreclosed asset and the related loan outstanding is recognised as a provision for loan losses in the Income Statement in the year of taking over the foreclosed properties in satisfaction of the debt. The Bank reviews these assets at each reporting date to assess whether an allowance for impairment should be recorded in the Income Statement.

Subsequent gains and losses on the disposal of the foreclosed assets are treated as provisions written back or charged to Income Statement, respectively.

**2.3 Finance Leases**

Assets leased to customers which transfer substantially all the risks and rewards associated with ownership other than legal title are accounted for as finance leases.

Amounts receivable under finance leases net of initial rentals received, unearned lease income and provision for rentals doubtful of recovery are classified as Lease Receivable in the Balance Sheet.

**2.3.1 Provision for Lease Receivable**

Specific provision has been made in relation to identified bad and doubtful leases.

In addition, a general provision for possible losses on Lease Receivable is made at 0.5% of the total Lease Receivable.

**2.4 Credit Card Receivable**

Amounts receivable on Credit Cards are included in Advances to Customers at the amounts expected to be recovered.

**2.4.1 Provision for Credit Card Receivable**

100% specific provision is made on Credit Card Receivable outstanding for 6 months and over.

In addition, a general provision is made at 3% on the capital included in Credit Card Receivable up to 6 months.

### 2.5 Government of Sri Lanka Treasury Bills and Bonds

#### 2.5.1 *Investments in Treasury Bills and Treasury Bonds held for Trading*

Investments in Treasury Bills and Treasury Bonds in the trading portfolio are marked to market and carried at that market value in the Balance Sheet. Gains and losses on mark to market valuation are dealt with through the Income Statement.

#### 2.5.2 *Investments in Treasury Bills and Bonds held to Maturity*

Investments in Treasury Bills and Bonds held to maturity are reflected at the value of the Bills/Bonds purchased and the discount/premium accrued thereon. Discount received/premium paid is taken to the Income Statement based on a pattern reflecting a constant periodic rate of return.

#### 2.5.3 *Securities Purchased under Resale Agreements*

These are advances collateralised by purchase of Treasury Bills and Treasury Bonds from the public subject to a commitment to resell them at a predetermined price. Such securities remain on the Balance Sheet of the Bank and the asset is recorded in respect of the consideration paid and interest accrued thereon.

### 2.6 Investments

#### 2.6.1 *Dealing Securities*

These are marketable securities acquired and held with the intention of resale over a short period of time. Such securities are carried at the market value at the Balance Sheet date.

#### 2.6.2 *Investments held for Sale*

These are investments classified as held for sale as at the Balance Sheet date. The Bank intends to recover the value of these assets principally through a sales transaction rather than through continuing to hold.

As per the Sri Lanka Accounting Standard No. 38 on Non-Current Assets Held for Sale and Discontinued Operations, these assets are measured at the lower of their carrying amount and fair value less costs to sell. Thereafter the Bank assesses at each Balance Sheet date whether there is objective evidence that an investment or a group of investments is impaired. The Bank recognises an impairment loss for any initial or subsequent write down of the assets to fair value less costs to sell and also recognises a gain for any subsequent increase in fair value less costs to sell of an asset, only to the extent of the cumulative impairment losses that have been recognised previously.

#### 2.6.3 *Investments held to Maturity*

These are acquired and held for yield or capital growth in the medium to long term. Such securities are recorded at cost. Changes in market values of these securities are not taken into account, unless there is considered to be a diminution in value which is other than temporary.

#### 2.6.4 *Investments in Associates*

Investments in associates are accounted for under the Cost Method in the Bank's Financial Statements and under the Equity Method in the Consolidated Financial Statements in accordance with the Sri Lanka Accounting Standard No. 27 on Accounting for Investments in Associates.

#### 2.6.5 *Investments in Subsidiaries*

Investments in subsidiaries are stated at cost in the Bank's Financial Statements in accordance with the Sri Lanka Accounting Standard No. 26 on Consolidated and Separate Financial Statements.

## 2.7 Investment Properties

The Group holds certain properties as investments to earn rental income, for capital appreciation or for both. Investment Properties are measured initially at cost, including transaction costs. Subsequent to initial recognition, Investment Properties are carried at cost.

## 2.8 Property, Plant & Equipment

**2.8.1** Property, Plant & Equipment are recorded at cost of purchase or construction or valuation together with any incidental expenses thereon. These assets are stated at cost/valuation less accumulated depreciation which is provided for on the basis specified in 2.8.2 below.

**2.8.2** Depreciation is provided at the following rates on straight-line basis over the periods appropriate to the estimated useful lives of the different types of assets:

Freehold and Leasehold buildings	2.5% per annum
Motor vehicles	20% per annum
Computer equipment	16.67% - 20.00% per annum
Office equipment	20% per annum
Furniture & fittings	10% per annum
Office Interior work	10% per annum
Machinery & Equipment	10% per annum

Depreciation is provided on a pro rata basis on the assets purchased/constructed/disposed of during the year. Depreciation is not provided for freehold land.

**2.8.3** An item of Property, Plant & Equipment is derecognised upon disposal or when no future economic benefits are expected from its use or disposal. Any gain or loss arising on derecognising of the asset (calculated as the difference between the net disposal proceeds and the carrying amount of the asset) is recognised in the Income Statement in the year the asset is derecognised.

**2.8.4** The revaluation surplus included in equity will be transferred to retained earnings when the underlying assets are sold.

## 2.9 Intangible Assets

### 2.9.1 Basis of Recognition

An Intangible Asset is recognised if it is probable that future economic benefits that are attributable to the asset will flow to the entity and the cost of the asset can be measured reliably in accordance with the Sri Lanka Accounting Standard No. 37 on Intangible Assets. Accordingly, these assets are stated in the Balance Sheet at cost less accumulated amortisation and accumulated impairment losses.

### 2.9.2 Subsequent Expenditure

Subsequent expenditure on Intangible Assets is capitalised only when it increases the future economic benefits embodied in these assets. All other expenditure is expensed as incurred.

### 2.9.3 Amortisation

The useful lives of intangible assets are assessed to be either finite or indefinite. Intangible assets with finite lives are amortised over the useful economic life. The amortisation period and the amortisation method for an intangible asset with a finite useful life are reviewed at least at each financial year end. Changes in the expected useful life or the expected pattern of consumption of future economic benefits

embodied in the asset are accounted for by changing the amortisation period or method, as appropriate and are treated as changes in accounting estimates. The amortisation expense on intangible assets with finite lives is recognised in the Income Statement.

### **2.9.4 Computer Software**

Computer Software is stated at cost less accumulated amortisation. Amortisation is done at 16.67% per annum on cost.

### **2.9.5 Copyright**

Cost of copyrights purchased are stated at cost less accumulated amortisation. Amortisation is done at 20% per annum on cost.

### **2.9.6 Impairment**

The unamortised balances of Intangible Assets with finite lives are reviewed at each Balance Sheet date for impairment whenever there is an indication for impairment and recognised as expenses in the Income Statement to the extent that they are no longer probable of being recovered from the expected future benefits.

Intangible assets with indefinite useful lives are tested for impairment annually either individually or at the cash generating unit level. Such intangibles are not amortised. The useful life of an intangible asset with an indefinite life is reviewed annually to determine whether indefinite life assessment continues to be supportable. If not, the change in the useful life assessment from indefinite to finite is made on a prospective basis.

Gains or losses arising from derecognition of an intangible asset are measured as the difference between the net disposal proceeds and the carrying amount of the asset and are recognised in the Income Statement when the asset is derecognised.

## **2.10 Impairment of Non-Financial Assets**

The Bank assesses at each reporting date or more frequently if events or changes in circumstances indicate that the carrying value may be impaired, whether there is an indication that a non-financial asset may be impaired. If any such indication exists, or when an annual impairment testing for an asset is required, the Bank makes an estimate of the asset's recoverable amount. When the carrying amount of an asset (or cash generating unit) exceeds its recoverable amount, the asset (or cash generating unit) is considered impaired and is written down to its recoverable amount.

For assets excluding goodwill, an assessment is made at each reporting date as to whether there is any indication that previously recognised impairment losses may no longer exist or may have decreased. If such condition exists, the recoverable amount is estimated. A previously recognised impairment loss is reversed only if there has been a change in the estimates used to determine the asset's recoverable amount since the last impairment loss was recognised. If that is the case, the carrying amount of the asset is increased to its recoverable amount.

### 3. Liabilities and Provisions

#### 3.1 Commitments and Contingencies

All discernible risks are accounted for in determining the amount of other liabilities. Bank's share of any contingencies and capital commitments of a subsidiary or an associate for which the Bank is also liable severally or otherwise is included with appropriate disclosures.

#### 3.2 Defined Benefit Plans (DBPs)

##### 3.2.1 Pensions and Retirement Benefits

###### 3.2.1.1 Description of the Plan and Employee Groups Covered

The Bank has an approved Pension Fund, which was established in 1992. As per the Deed of Trust, only those employees who were less than 45 years of age as at January 1, 1992 are covered by the Pension Fund in order to leave a minimum contribution for a period of 10 years before they are eligible to draw pension from the Pension Fund. Only the employees who joined the Bank on or before December 31, 2001 are in pensionable service of the Bank. The pensions paid to those employees who retired on or before December 31, 2001 and on whose behalf the Bank could not make contributions to the Pension Fund for more than 10 years, is charged to the Income Statement.

###### 3.2.1.2 Surplus in the Pension Fund/Unfunded Pension Liability

The results revealed that the fair value of the fund's assets is Rs. 2,545.294 million and that the actuarial present value of the promised retirement benefits is Rs. 3,866.606 million resulting in a deficit of Rs. 1,321.312 million, as at August 31, 2006 (a surplus of Rs. 226.322 million as at December 31, 2005) in the Pension Fund and the Widows' & Orphans' Pension Scheme due to the changes in actuarial assumptions (i.e. interest rates, salary increases etc.) that took place since the previous actuarial valuation as at December 31, 2005.

As detailed in 3.3.1 below, the Bank offered a restructured pension scheme aimed at converting the DBP to a Defined Contribution Plan (DCP) to the pensionable employees of the Bank during the year and over 99% of them accepted it. As a result, the above Pension Fund now covers only the staff who did not opt for the restructured pension scheme and those employees who retired before the restructured pension scheme came into effect. The Bank incurred an initial cost of Rs. 1.654 billion on account of this conversion.

###### 3.2.1.3 Funding Arrangements

The Bank contributes to the Pension Fund and the Widows' & Orphans' Pension Scheme monthly based on a percentage of gross emoluments excluding certain allowances and bonus of the pensionable employees who did not opt for the restructured pension scheme. The percentages of contribution are as recommended by the Actuary. The Pension Fund is non-contributory while employees contribute 75% of the recommended contribution rate to the Widows' & Orphans' Pension Scheme.

###### 3.2.1.4 Actuarial Valuation and Actuarial Valuation Method

An actuarial valuation is undertaken at least every three years to ascertain the full liability. The liability is calculated on an ongoing basis.

An actuarial valuation of the Pension Fund and the Widows' & Orphans' Pension Scheme was carried out as at August 31, 2006 by M/s. Hewitt Outsourcing Services (India) Ltd. The valuation has been carried out based on the Projected Unit Credit method, the benchmark treatment recommended by the Sri Lanka Accounting Standard No. 16 on Retirement Benefits Costs.

### *3.2.1.5 Principal Actuarial Assumptions*

The principal financial assumptions used in the Valuation are as follows:

Long-term rate of interest	9.0% per annum
Salary increases	10.0% per annum

The demographic assumptions underlying the valuation are retirement age (55 or 60 years), early withdrawals from service, retirement on medical grounds, death before and after retirement, etc.

The recommended contribution rate for the future has been suggested based on the above assumptions.

### *3.2.1.6 Management of the Fund's Assets*

The assets of the Pension Fund and the Widows' & Orphans' Pension Scheme are held separately from those of the Bank and are independently administered by the Trustees as per the provisions of the Trust Deed.

### **3.2.2 Gratuity**

Provision has not been made in these Financial Statements for gratuity payable under the Payment of Gratuity Act No. 12 of 1983 to those employees who joined the Bank on or before December 31, 2001, as they are either in pensionable service of the Bank under the DBP and that the Bank has its own non-contributory retirement pension scheme in force for them or has a DCP as explained in 3.3.1 below. However, if any of these employees who are eligible for gratuity resigns before retirement the Bank is liable to pay gratuity to such employees.

Provision has been made in these Financial Statements for retirement gratuities from the first year of service for all the employees who joined the Bank on or after January 1, 2002, as they are not in pensionable service of the Bank, in conformity with the Sri Lanka Accounting Standard No.16 on Retirement Benefits Costs. However, under the Payment of Gratuity Act No.12 of 1983, the liability to an employee arises only on completion of 5 years of continued service. The gratuity liability is unfunded and an actuarial valuation has not been carried out.

### **3.3 Defined Contribution Plans (DCPs)**

Contributions to defined contribution pension plans are recognised as an expense in the Income Statement as incurred.

#### **3.3.1 Defined Contribution Pension Plans**

During the year, the Bank restructured its pension scheme which was a Defined Benefit Plan (DBP) to a Defined Contribution Plan (DCP). This restructured plan was offered on a voluntary basis to the eligible employees of the Bank. The scheme provides for lump sum payments instead of commuted / monthly pensions to the eligible employees at the point of their separation, in return for surrendering their pension rights. The lump sum offered consisted of a past service package and a future service package. The cost to be incurred on account of the past service package in excess of the funds available in the Pension Fund was borne by the Bank.

The future service package includes monthly contributions to be made by the Bank for the employees who accepted the offer, to be made during their remaining period of service, at pre-determined contribution rates to be applied on their salaries, estimated to increase for this purpose at 10% p.a. In addition, actual interest to be earned by the Pension Fund will also be allocated on a pro rata basis to the employees who joined the new scheme.

With the implementation of the new scheme, the Bank was able to change the basis of the previous pension scheme from a DBP to a DCP and prevent the future funding deficiencies in the Fund on account of the employees who accepted the offer.

**3.3.2 Employees' Provident Fund**

The Bank and employees contribute to the approved private Provident Fund at 12% and 8% respectively.

**3.3.3 Employees' Trust Fund**

The Bank contributes to the Employees' Trust Fund at 3%.

**3.4 Securities sold under Repurchase Agreements**

These are borrowings collateralised by sale of Treasury Bills and Treasury Bonds held by the Bank to the counterparty from whom the Bank borrowed, subject to a commitment to repurchase them at a pre-determined price. Such securities remain on the Balance Sheet of the Bank and the liability is recorded in respect of the consideration received and interest accrued thereon.

**3.5 Provisions for Liabilities**

A provision is recognised in the Balance Sheet when the Bank has a legal or constructive obligation as a result of a past event, and it is probable that an outflow of economic benefits will be required to settle the obligations, in accordance with the Sri Lanka Accounting Standard No. 36 on Provisions, Contingent Liabilities and Contingent Assets.

**4. Income Statement****4.1 Revenue Recognition****4.1.1 Interest Income**

In terms of the provisions of the Sri Lanka Accounting Standard No. 23 on Revenue Recognition and Disclosures in the Financial Statements of Banks, the interest receivable is recognised on accrual basis. Interest ceases to be taken into revenue when the recovery of interest and/or principal is in arrears for three months. Interest receivable on advances classified as non-performing is accounted for on cash basis. Interest falling due on non-performing advances is credited to Interest in Suspense Account. In addition, interest accrued up to three months on such non-performing advances is also eliminated from the interest income and transferred to interest in suspense.

**4.1.2 Lease Income**

In terms of the provisions of the Sri Lanka Accounting Standard No. 19 on Leases, the recognition of finance income on leasing is accounted based on a pattern reflecting a constant periodic rate of return on capital outstanding.

The excess of aggregate lease rentals receivable over the cost of the leased assets constitutes the total unearned finance income at the commencement of a lease. The unearned finance income included in the lease rentals receivable is taken into revenue over the term of the lease commencing from the month in which the lease is executed in proportion to the capital outstanding.

Finance income in respect of lease rentals due ceases to be taken to revenue when they are in arrears for three months. Thereafter such income is recognised on cash basis. Interest accrued up to three months on such non-performing leases is also eliminated from the interest income and transferred to interest in suspense.

#### **4.1.3 Income on Discounting of Bills of Exchange**

Income on discounting of Bills of Exchange is recognised proportionately over the period of the instrument.

#### **4.1.4 Fees and Commission Income**

The Bank earns fees and commission income from a diverse range of services it provides to its customers. This includes fees and commission income arising on financial services provided by the Group including Trade Finance, Travel, Investment Banking, e-Banking, money remittance, Credit Cards, Legal etc. Fees and commission income other than fees receivable on credit cards are recognised on cash basis.

#### **4.1.5 Dividend Income on Shares and Units**

Dividend income from shares and units is recognised when the Bank's right to receive the payment is established.

#### **4.1.6 Interest Income on Investments in Debentures and Trust Certificates**

Interest income on investments in Debentures and Trust Certificates is recognised on accrual basis.

#### **4.1.7 Rental Income**

Rental income is recognised on accrual basis.

#### **4.1.8 Interest and Fees Receivable on Credit Cards**

Interest and fees receivable on Credit Cards are recognised on accrual basis. Interest and fees cease to be taken into revenue when the recovery of interest or fees is in arrears for three months. Thereafter, interest and fees are accounted for on cash basis.

#### **4.1.9 Gains and Losses on Disposal of Property, Plant & Equipment, Non-Current Investments held for Sale, Dealing Securities, Investment Securities and Foreclosed Properties**

Gains and losses resulting from the disposal of Property, Plant & Equipment, Non-Current investments held for Sale, Dealing Securities, Investment Securities and Foreclosed Properties have been accounted for on cash basis in the Income Statement.

### **4.2 Interest and Other Expenses**

In terms of the provisions of the Sri Lanka Accounting Standard No. 23 on Revenue Recognition and Disclosures in the Financial Statements of Banks, the interest and other expenses payable are recognised on accrual basis in the Income Statement.

### **4.3 Borrowing Costs**

Costs incurred in respect of funds specifically obtained for the acquisition of the Property, Plant & Equipment have been recognised as an expense in the Income Statement in the period in which they are incurred, in terms of the Sri Lanka Accounting Standard No. 20 on Borrowing Costs.

**4.4 Terminal Benefits**

The actual amounts paid as pension and retirement gratuities to those employees, who are not covered by the Pension Funds as per 3.2.1 and 3.3.1 above, are charged to the Income Statement. The actual amounts paid as pension to those employees who are covered by the Pension Fund are borne by the Retirement Pension Fund.

**4.5 Off-Balance Sheet Transactions**

The Bank enters into Off-Balance Sheet transactions such as forward exchange contracts. At the year end, unrealised gains and losses are dealt with through the Income Statement.

**5. Cash Flow Statement**

The Cash Flow Statement has been prepared by using the 'Direct Method' of preparing cash flows in accordance with the Sri Lanka Accounting Standard No. 9 on Cash Flow Statements. Cash and cash equivalents comprise mainly of cash balances, loans at call and short-term placements/balances with foreign banks.

**6. Segment Reporting**

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

In accordance with the Sri Lanka Accounting Standard No. 28 on Segment Reporting, segmental information is presented in respect of the Group. The segments comprise of banking, leasing, dealing and property/investment.

Inter-segment transactions are based on fair market prices.

Segment results, assets and liabilities include items directly attributable to a segment as well as those that can be allocated on a reasonable basis. Unallocated items comprise mainly of Head Office expenses.

Segment capital expenditure is the total cost incurred during the period to acquire segment assets that are expected to be used for more than one accounting period.

**7. Fiduciary Assets**

Assets held in a fiduciary capacity are not reported in these Financial Statements as they are not the assets of the Bank.

**8. Dividends on Ordinary and Preference Shares**

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

Dividends on ordinary shares for the year that are recommended by the Directors after the Balance Sheet date for approval of the shareholders at the Annual General Meeting are disclosed in Note 11 to the Financial Statements.

Dividends on preference shares are accrued in the Financial Statements.

**9. Directors' Responsibility Statement**

The Board of Directors takes the responsibility for the preparation and presentation of these Financial Statements. Please refer page 92 for the Statement of Directors' Responsibility for Financial Reporting.

**1. Interest Income**

	Bank		Group	
	2006 Rs.'000	2005 Rs.'000	2006 Rs.'000	2005 Rs.'000
Cash and short-term funds	235,349	140,457	235,349	140,457
Treasury Bills, Treasury Bonds and other Money Market instruments	2,593,469	978,129	2,612,078	1,249,483
Due from Banks	677,551	868,900	677,551	868,900
Customer advances	16,025,379	11,046,384	16,011,978	11,034,611
Other	-	-	272	367
	<b>19,531,748</b>	<b>13,033,870</b>	<b>19,537,228</b>	<b>13,293,818</b>

Since April 1, 2002, net interest income from Treasury Bills and Treasury Bonds has been grossed up by adding the notional tax credit, consequent to the interest income on Treasury Bills and Treasury Bonds being subjected to withholding tax as detailed in Note 9.1.

**2. Interest Expenses**

Cash and short-term funds	202,013	159,185	202,013	159,185
Due to Banks	461,517	171,975	461,517	171,975
Repurchase agreements and other Money Market instruments	1,396,043	766,883	1,395,157	1,005,825
Customer deposits	9,025,190	5,568,394	9,016,132	5,561,822
Debentures issued	641,540	371,049	641,540	371,049
Refinance borrowings	228,307	188,574	228,307	188,574
	<b>11,954,610</b>	<b>7,226,060</b>	<b>11,944,666</b>	<b>7,458,430</b>

**3. Fees and Commission Income**

Trade and other related activities	863,666	772,463	863,666	772,463
Personal banking	191,012	139,827	190,918	139,742
Foreign remittances	52,538	22,001	52,538	22,001
Electronic banking	333,374	253,339	333,374	253,339
Professional services	89,096	91,855	89,096	91,855
Other	481,599	480,219	481,599	480,219
	<b>2,011,285</b>	<b>1,759,704</b>	<b>2,011,191</b>	<b>1,759,619</b>

**4. Other Income**

	<b>Bank</b>		<b>Group</b>	
	<b>2006</b>	2005	<b>2006</b>	2005
	<b>Rs. '000</b>	Rs. '000	<b>Rs. '000</b>	Rs. '000
Income from investment securities (quoted)	<b>41,153</b>	50,410	<b>41,153</b>	50,410
Income from investment securities (unquoted)	<b>204,823</b>	248,533	<b>205,528</b>	249,287
Income from investments in associates (quoted)	<b>9,555</b>	21,270	<b>9,555</b>	21,270
Income from investments in associates (unquoted)	<b>1,830</b>	3,264	<b>1,830</b>	3,264
Income from investments in subsidiaries (quoted)	<b>36,760</b>	11,232	-	-
Income from investments in subsidiaries (unquoted)	-	95,850	-	-
Income from Unit Trust Company	<b>11,377</b>	10,113	<b>11,377</b>	10,113
Bad debts recovered				
(including recovery of debts written-off)	<b>252,493</b>	198,949	<b>252,493</b>	198,949
Profit on sale of Property, Plant & Equipment	<b>3,871</b>	31,008	<b>8,163</b>	33,323
Rental and other income	<b>118,168</b>	24,973	<b>128,771</b>	44,315
Gain/(Loss) on Mark to Market Valuation on shares/ Realised Profit/(Loss) on sale of shares	<b>802,669</b>	63,213	<b>802,669</b>	63,213
Gains/(Losses) on Mark to Market Valuation on Treasury Bills and Bonds/Realised Profit/(Loss) on sale of Treasury Bills and Bonds	<b>4,730</b>	(39,659)	<b>4,730</b>	(64,585)
	<b>1,487,429</b>	719,156	<b>1,466,269</b>	609,559
Less: Dividends received from associate companies transferred to the Investments in Associate Companies Account	-	-	<b>1,830</b>	24,534
	<b>1,487,429</b>	719,156	<b>1,464,439</b>	585,025

**5. Operating Expenses**

Operating expenses include the following:

Directors' emoluments	<b>33,074</b>	27,851	<b>33,204</b>	27,977
Auditors' remuneration	<b>5,148</b>	3,814	<b>5,513</b>	4,037
Non-Audit fees	<b>2,402</b>	1,056	<b>2,402</b>	1,150
Terminal benefits	<b>17,832</b>	18,253	<b>17,832</b>	18,253
Pensions paid to past Directors	<b>1,897</b>	1,881	<b>1,897</b>	1,881
Depreciation/amortisation	<b>375,779</b>	299,167	<b>409,613</b>	328,868
Professional and legal expenses	<b>96,166</b>	50,169	<b>96,382</b>	50,362
Advertising and marketing	<b>140,377</b>	126,750	<b>140,377</b>	126,750
Donations	<b>3,442</b>	1,348	<b>3,442</b>	1,348
Donation to Coporate Social Responsibility (CSR) Trust	<b>10,063</b>	8,500	<b>10,063</b>	8,500
Employer's contribution to Employees' Provident Fund	<b>138,699</b>	117,658	<b>139,821</b>	118,642
Employer's contribution to Employees' Trust Fund	<b>33,453</b>	28,108	<b>33,734</b>	28,353
Gratuity provision/paid	<b>26,644</b>	14,711	<b>28,049</b>	15,203
Financial Value Added Tax (VAT) on profits	<b>970,958</b>	622,936	<b>970,958</b>	624,605

**6. Provision for Staff Retirement Benefits**

A sum of Rs. 1,813.835 million (Rs. 235.971 million in 2005) has been charged against profits being the total contributions for the year to the approved Pension Fund and Widows' & Orphans' Pension Scheme.

**7. Loan Losses and Provisions**

	<b>Bank</b>		<b>Group</b>	
	<b>2006</b>	2005	<b>2006</b>	2005
	<b>Rs.'000</b>	Rs.'000	<b>Rs.'000</b>	Rs.'000
Provision for bad & doubtful debts:				
Specific provision on Bills of Exchange	<b>1,058</b>	979	<b>1,058</b>	979
Specific provision on loans and advances	<b>418,637</b>	348,042	<b>418,637</b>	348,042
General provision on loans and advances	<b>128,617</b>	20,034	<b>128,617</b>	20,034
Specific provision on credit card receivables	<b>17,274</b>	4,103	<b>17,274</b>	4,103
General provision on credit card receivables	<b>10,763</b>	7,671	<b>10,763</b>	7,671
Specific provision on lease receivable	<b>58,778</b>	20,449	<b>58,778</b>	20,449
General provision on lease receivable	<b>12,245</b>	8,575	<b>12,245</b>	8,575
Total provisions made during the year	<b>647,372</b>	409,853	<b>647,372</b>	409,853
Direct write-offs	<b>7,698</b>	5,011	<b>7,698</b>	5,011
	<b>655,070</b>	414,864	<b>655,070</b>	414,864

**8. Share of Profit/(Loss) before Tax of Associate Companies**

Commercial Leasing Co. Ltd.	-	-	<b>54,687</b>	93,820
Equity Investments Lanka Ltd.	-	-	<b>2,446</b>	1,265
Commercial Fund Management (Pvt) Ltd.	-	-	<b>5,321</b>	5,377
	-	-	<b>62,454</b>	100,462

**9. Provision for Taxation**

**9.1 Charge to taxation is as follows:**

**Bank**

Income tax on profits for the year	<b>2,191,641</b>	1,339,103	<b>2,191,641</b>	1,339,103
Over provision for taxation in previous years	-	(37,129)	<b>(2,773)</b>	(76,173)
Transfer/(Reversal) to deferred taxation	<b>9,276</b>	(24,254)	<b>9,276</b>	(24,254)
	<b>2,200,917</b>	1,277,720	<b>2,198,144</b>	1,238,676

**Subsidiary Companies**

Income tax on profits of				
Commercial Development Co. Ltd.	-	-	<b>24,044</b>	17,703
Income tax on profits of Commercial Bank				
Primary Dealer Ltd.	-	-	<b>6,797</b>	7,144
Income tax on profits of ONEzero Co. Ltd.	-	-	<b>45</b>	-
Income tax on profits of X-pertise Ltd.	-	-	<b>629</b>	191

**Associate Companies**

Income tax on profits of				
Commercial Leasing Co. Ltd.	-	-	<b>13,022</b>	29,977
Income tax on profits of				
Equity Investments Lanka Ltd.	-	-	<b>170</b>	23
Income tax on profits of				
Commercial Fund Management (Pvt) Ltd.	-	-	<b>1,787</b>	1,938

**WHT deducted on dividend payments by subsidiary and associate companies**

	-	-	<b>4,113</b>	14,317
	<b>2,200,917</b>	1,277,720	<b>2,248,751</b>	1,309,969

Income tax has been provided on the taxable income at the following rates:

	2006	2005
Domestic operations of the Bank	35.00%	30.00%
On-shore banking operations of the Off-Shore Banking Centre of the Bank	35.00%	30.00%
Off-shore banking operations of the Off-Shore Banking Centre of the Bank	20.00%	20.00%
Operations of the Bangladesh branches	45.00%	45.00%
Commercial Development Co. Ltd.	35.00%	30.00%
Commercial Bank Primary Dealer Ltd.	35.00%	32.50%
ONEzero Co. Ltd. (for IT related services)	-	-
X-pertise Ltd.	15.00%	20.00%

#### Notional Tax Credit for Withholding Tax on Government Securities on Secondary Market Transactions

The Inland Revenue (Amendment) Act No. 19 of 2003, provides that a company which derives interest income from the secondary market transactions in Government securities (on or after April 1, 2002) would be entitled to a notional tax credit (being one ninth of the net interest income) provided such interest income forms part of the statutory income of the Company for that year of assessment.

Accordingly, the net interest income earned by the Bank and Commercial Bank Primary Dealer Ltd. from the secondary market transactions in Government securities for the year, has been grossed up in the Financial Statements and the resulting notional tax credit amounts to Rs. 15.755 million (Rs. 11.095 million in 2005) and Rs. 1.950 million (Rs. 3.010 million in 2005) respectively.

#### 9.2 Reconciliation of Accounting Profit and Taxable Income:

	2006	2005
	Rs.'000	Rs.'000
Net profit as per the Income Statement	4,213,545	3,641,960
Add: Non-deductible expenses	7,761,792	4,600,143
	<b>11,975,337</b>	8,242,103
Less: Deductible expenses	4,435,674	3,604,812
Less: Exempt income	1,647,510	414,034
Statutory income from business	<b>5,892,153</b>	4,223,257
Less: Dividend/Interest from primary market activities	96,002	190,169
Add: Non-business income	114,895	53,310
Assessable income	<b>5,911,046</b>	4,086,398
Less: Qualifying payments	3,432	663
Taxable income	<b>5,907,614</b>	4,085,735
Income tax provision for the year is made up as follows:		
Income tax on profit of the Domestic Banking Unit	1,659,172	891,601
Income tax on profit of the Off-Shore Banking Centre	105,954	106,084
Income tax on profit of the operations of Bangladesh branches	426,515	341,418
Over provision for taxation in previous years	-	(37,129)
Provision for/(Reversal of) deferred tax	9,276	(24,254)
	<b>2,200,917</b>	1,277,720
Effective tax rate (excluding deferred tax)	<b>52.01%</b>	35.43%

### 10. Earnings per Ordinary Share

Basic earnings per ordinary share is calculated by dividing the net profit attributable to ordinary shareholders after deducting dividends on Preference Shares by the weighted average number of ordinary shares in issue (both voting and non-voting) during the year as required by the Sri Lanka Accounting Standard No. 34 on Earnings per Share. The corresponding figures for the previous years have been adjusted accordingly.

Diluted earnings per ordinary share is calculated by dividing the net profit attributable to ordinary shareholders after deducting dividends on Preference Shares by the weighted average number of ordinary shares outstanding during the year plus the weighted average number of ordinary shares that would be issued on the conversion of all the dilutive potential ordinary shares into ordinary shares.

	Bank		Group	
	2006 Rs. '000	2005 Rs. '000	2006 Rs. '000	2005 Rs. '000
Profit after taxation and minority interest	<b>2,012,628</b>	2,364,240	<b>2,070,707</b>	2,356,438
Less: Dividends on Cumulative Redeemable Preference Shares	<b>197,418</b>	230,352	<b>197,418</b>	230,352
Profit attributable to Ordinary Shareholders	<b>1,815,210</b>	2,133,888	<b>1,873,289</b>	2,126,086
Number of Ordinary Shares used as Denominator	<b>142,818,724</b>	142,818,724	<b>142,818,724</b>	142,818,724
Effect of dilution:				
Dilutive potential ordinary shares under Employee Share Option Plan (Refer Note 30)	<b>4,760,203</b>	4,760,203	<b>4,760,203</b>	4,760,203
Less: Exercised Ordinary Shares under Employee Share Option Plan (Refer Note 30)	<b>(2,129,016)</b>	(2,129,016)	<b>(2,129,016)</b>	(2,129,016)
Number of Ordinary Shares including dilutive Ordinary Shares used as Denominator	<b>145,449,911</b>	145,449,911	<b>145,449,911</b>	145,449,911
Basic Earnings per Ordinary Share (Rs.)	<b>12.71</b>	14.94	<b>13.12</b>	14.89
Diluted Earnings per Ordinary Share (Rs.)	<b>12.48</b>	14.67	<b>12.88</b>	14.62

### 11. Dividends

	Bank		Group	
	2006 Rs. '000	2005 Rs. '000	2006 Rs. '000	2005 Rs. '000
<b>On Ordinary Shares</b>				
Net dividend paid to the Shareholders	<b>202,185</b>	201,979	<b>202,185</b>	201,979
Withholding tax deducted at source	<b>11,944</b>	11,142	<b>11,944</b>	11,142
Gross dividend	<b>214,129</b>	213,121	<b>214,129</b>	213,121
<b>On Preference Shares</b>				
Dividend paid/payable on Cumulative Redeemable Preference Shares of Rs. 10/- each for the period/year				
Net dividend paid/payable	<b>177,676</b>	207,317	<b>177,676</b>	207,317
Withholding tax deducted/to be deducted at source	<b>19,742</b>	23,035	<b>19,742</b>	23,035
Gross dividend	<b>197,418</b>	230,352	<b>197,418</b>	230,352
Total dividend	<b>411,547</b>	443,473	<b>411,547</b>	443,473

15% interim dividend paid in November 2006 to the Ordinary Shareholders was partly paid out of the exempt dividends received by the Bank. The effective interim dividend rate was 15.09% for the year (15.60% for 2005).

Directors have recommended the payment of a final dividend of 35% for the year ended December 31, 2006 (30% in 2005) which will be declared at the Annual General Meeting to be held on March 28, 2007. In accordance with the Sri Lanka Accounting Standard No. 12 (Revised) on Events after the Balance Sheet Date, this proposed final dividend has not been recognised as a liability as at the year end.

Dividend on the 13% Cumulative Redeemable Preference shares was paid on September 20, 2006, the date of redemption.

**12. Unappropriated Profit/(Loss) carried forward**

	Bank		Group	
	2006 Rs. '000	2005 Rs. '000	2006 Rs. '000	2005 Rs. '000
Commercial Bank of Ceylon Ltd.	500,521	427,238	426,310	353,027
<b>Subsidiary Companies:</b>				
Commercial Development Co. Ltd.	-	-	(8,952)	30,300
Commercial Bank Primary Dealer Ltd.	-	-	56,757	41,451
ONEzero Co. Ltd.	-	-	19,242	11,828
X-pertise Ltd.	-	-	463	(705)
<b>Associate Companies:</b>				
Commercial Leasing Co. Ltd.	-	-	174,154	174,327
Equity Investments Lanka Ltd.	-	-	(3,366)	(4,409)
Commercial Fund Management (Pvt) Ltd.	-	-	8,713	5,790
	<b>500,521</b>	<b>427,238</b>	<b>673,321</b>	<b>611,609</b>

**13. Cash and Short-Term Funds**

Coins and notes held in local currency	2,677,172	2,305,679	2,669,902	2,299,585
Coins and notes held in foreign currency	605,186	257,177	605,186	257,177
Due from Banks	8,506,479	15,723,987	8,506,479	15,723,987
Loans at call and short notice	1,949,872	376,010	1,949,872	376,010
	<b>13,738,709</b>	<b>18,662,853</b>	<b>13,731,439</b>	<b>18,656,759</b>

**14. Balances with Central Banks**

Bank's Current Account with Central Bank of Sri Lanka	9,942,248	7,307,846	9,942,248	7,307,846
Bank's Current Account with Bangladesh Bank	2,631,403	1,737,334	2,631,403	1,737,334
	<b>12,573,651</b>	<b>9,045,180</b>	<b>12,573,651</b>	<b>9,045,180</b>

As required by the provisions of Section 93 of the Monetary Law Act, a cash balance is maintained with the Central Bank of Sri Lanka. As at December 31, 2006 the minimum cash reserve requirement was 10% of the rupee deposit liabilities. There is no reserve requirement for foreign currency deposit liabilities of the Domestic Banking Unit and the deposit liabilities of the Off-Shore Banking Centre.

As per the Bangladesh Bank regulations, the Statutory Liquid Assets Requirement is 18% on time and demand liabilities, which includes 5% as cash reserve requirement and the balance 13% can be maintained in foreign currency held with the Bangladesh Bank and/or in unencumbered securities.

**15. Government Treasury Bills and Bonds**

	Bank		Group	
	2006 Rs. '000	2005 Rs. '000	2006 Rs. '000	2005 Rs. '000
Government Treasury Bills and Bonds held for trading	3,259,651	3,119,159	3,259,651	3,119,159
Government Treasury Bills and Bonds held to maturity	8,780,658	8,290,924	8,962,120	8,546,337
	<b>12,040,309</b>	<b>11,410,083</b>	<b>12,221,771</b>	<b>11,665,496</b>

## Notes to the Financial Statements

### 16. Dealing Securities

	Bank				Group			
	As at 31.12.06		As at 31.12.05		As at 31.12.06		As at 31.12.05	
	Cost Rs.'000	Market Value Rs.'000	Cost Rs.'000	Market Value Rs.'000	Cost Rs.'000	Market Value Rs.'000	Cost Rs.'000	Market Value Rs.'000
<b>Quoted</b>								
<b>SHARES</b>								
Nations Trust Bank Ltd. (175,000 Ordinary Shares of Rs.10/- each) (150,000 Ordinary Shares of Rs.10/- each as at December 31, 2005)	<b>4,547</b>	<b>4,944</b> (@ Rs. 28.25)	3,830	3,525 (@ Rs. 23.50)	<b>4,547</b>	<b>4,944</b> (@ Rs. 28.25)	3,830	3,525 (@ Rs. 23.50)
Merchant Bank of Sri Lanka Ltd. (153,614 Ordinary Shares of Rs.10/- each) (153,614 Ordinary Shares of Rs.10/- each as at December 31, 2005)	<b>4,627</b>	<b>2,343</b> (@ Rs. 15.25)	4,627	2,189 (@ Rs. 14.25)	<b>4,627</b>	<b>2,343</b> (@ Rs. 15.25)	4,627	2,189 (@ Rs. 14.25)
HDFC Bank of Sri Lanka (38,000 Ordinary Shares of Rs.100/- each) (38,000 Ordinary Shares of Rs.100/- each as at December 31, 2005)	<b>8,493</b>	<b>6,641</b> (@ Rs. 174.75)	8,493	7,258 (@ Rs. 191.00)	<b>8,493</b>	<b>6,641</b> (@ Rs. 174.75)	8,493	7,258 (@ Rs. 191.00)
Haycarb Ltd. (100,000 Ordinary Shares of Rs.10/- each) (100,000 Ordinary Shares of Rs.10/- each as at December 31, 2005)	<b>4,353</b>	<b>3,700</b> (@ Rs. 37.00)	4,353	3,325 (@ Rs. 33.25)	<b>4,353</b>	<b>3,700</b> (@ Rs. 37.00)	4,353	3,325 (@ Rs. 33.25)
John Keells Holdings Ltd. (60,000 Ordinary Shares of Rs.10/- each) (127,300 Ordinary Shares of Rs.10/- each as at December 31, 2005)	<b>11,783</b>	<b>11,700</b> (@ Rs. 195.00)	19,308	16,454 (@ Rs. 129.25)	<b>11,783</b>	<b>11,700</b> (@ Rs. 195.00)	19,308	16,454 (@ Rs. 129.25)
Hemas Holdings Ltd. (65,150 Ordinary Shares of Rs.10/- each) (81,650 Ordinary Shares of Rs.10/- each as at December 31, 2005)	<b>6,670</b>	<b>7,606</b> (@ Rs. 116.75)	8,375	8,471 (@ Rs. 103.75)	<b>6,670</b>	<b>7,606</b> (@ Rs. 116.75)	8,375	8,471 (@ Rs. 103.75)
Richard Pieris & Co. Ltd. (112,400 Ordinary Shares of Rs.10/- each) (112,400 Ordinary Shares of Rs.10/- each as at December 31, 2005)	<b>9,936</b>	<b>8,767</b> (@ Rs. 78.00)	9,936	7,615 (@ Rs. 67.75)	<b>9,936</b>	<b>8,767</b> (@ Rs. 78.00)	9,936	7,615 (@ Rs. 67.75)
Aitken Spence Hotel Holdings Ltd. (100,000 Ordinary Shares of Rs.10/- each) (100,000 Ordinary Shares of Rs.10/- each as at December 31, 2005)	<b>9,867</b>	<b>7,850</b> (@ Rs. 78.50)	9,867	6,800 (@ Rs. 68.00)	<b>9,867</b>	<b>7,850</b> (@ Rs. 78.50)	9,867	6,800 (@ Rs. 68.00)
Asian Hotels Properties Ltd. (150,000 Ordinary Shares of Rs.10/- each) (342,100 Ordinary Shares of Rs.10/- each as at December 31, 2005)	<b>6,335</b>	<b>7,650</b> (@ Rs. 51.00)	14,491	14,197 (@ Rs. 41.50)	<b>6,335</b>	<b>7,650</b> (@ Rs. 51.00)	14,491	14,197 (@ Rs. 41.50)
Connaissance Holdings Ltd. (411,000 Ordinary Shares of Rs.10/- each) (342,500 Ordinary Shares of Rs.10/- each as at December 31, 2005)	<b>14,924</b>	<b>15,207</b> (@ Rs. 37.00)	14,924	12,844 (@ Rs. 37.50)	<b>14,924</b>	<b>15,207</b> (@ Rs. 37.00)	14,924	12,844 (@ Rs. 37.50)
The Fortress Resorts Ltd. (174,893 Ordinary Shares of Rs.10/- each) (99,939 Ordinary Shares of Rs.10/- each as at December 31, 2005)	<b>2,609</b>	<b>1,924</b> (@ Rs. 11.00)	1,860	1,249 (@ Rs. 12.50)	<b>2,609</b>	<b>1,924</b> (@ Rs. 11.00)	1,860	1,249 (@ Rs. 12.50)
Eden Hotel Lanka Ltd. (100,000 Ordinary Shares of Rs.10/- each) (100,000 Ordinary Shares of Rs.10/- each as at December 31, 2005)	<b>2,273</b>	<b>1,200</b> (@ Rs. 12.00)	2,273	1,150 (@ Rs. 11.50)	<b>2,273</b>	<b>1,200</b> (@ Rs. 12.00)	2,273	1,150 (@ Rs. 11.50)

## Notes to the Financial Statements

	Bank				Group			
	As at 31.12.06		As at 31.12.05		As at 31.12.06		As at 31.12.05	
	Cost Rs.'000	Market Value Rs.'000						
Taj Lanka (250,400 Ordinary Shares of Rs.10/- each) (250,400 Ordinary Shares of Rs.10/- each as at December 31, 2005)	4,740	2,942 (@ Rs. 11.75)	4,740	3,005 (@ Rs. 12.00)	4,740	2,942 (@ Rs. 11.75)	4,740	3,005 (@ Rs. 12.00)
Colombo Land & Development Co. Ltd. (400,000 Ordinary Shares of Rs.1/- each) (300,000 Ordinary Shares of Rs.1/- each as at December 31, 2005)	2,643	1,760 (@ Rs. 4.40)	2,187	900 (@ Rs. 3.00)	2,643	1,760 (@ Rs. 4.40)	2,187	900 (@ Rs. 3.00)
C T Land & Development Ltd. (109,800 Ordinary Shares of Rs.10/- each) (109,800 Ordinary Shares of Rs.10/- each as at December 31, 2005)	1,505	1,565 (@ Rs. 14.25)	1,505	1,318 (@ Rs. 12.00)	1,505	1,565 (@ Rs. 14.25)	1,505	1,318 (@ Rs. 12.00)
Tokyo Cement Co. (Lanka) Ltd. (400,000 Non-Voting Ordinary Shares of Rs.1/- each) (350,000 Non-Voting Ordinary Shares of Rs.1/- each as at December 31, 2005)	6,910	6,800 (@ Rs. 17.00)	6,174	4,200 (@ Rs. 12.00)	6,910	6,800 (@ Rs. 17.00)	6,174	4,200 (@ Rs. 12.00)
Ceylon Glass Co. Ltd. (800,000 Ordinary Shares of Rs.1/- each) (800,000 Ordinary Shares of Rs.1/- each as at December 31, 2005)	4,063	1,920 (@ Rs. 2.40)	4,063	1,800 (@ Rs. 2.25)	4,063	1,920 (@ Rs. 2.40)	4,063	1,800 (@ Rs. 2.25)
Dankotuwa Porcelain Ltd. (83,333 Ordinary Shares of Rs.10/- each) (50,000 Ordinary Shares of Rs.10/- each as at December 31, 2005)	1,348	833 (@ Rs. 10.00)	1,014	750 (@ Rs. 15.00)	1,348	833 (@ Rs. 10.00)	1,014	750 (@ Rs. 15.00)
Dipped Products Ltd. (67,100 Ordinary Shares of Rs.10/- each) (67,100 Ordinary Shares of Rs.10/- each as at December 31, 2005)	6,317	7,247 (@ Rs. 108.00)	6,317	5,033 (@ Rs. 75.00)	6,317	7,247 (@ Rs. 108.00)	6,317	5,033 (@ Rs. 75.00)
Royal Ceramics Ltd. (700,000 Ordinary Shares of Rs.1/- each) (700,000 Ordinary Shares of Rs.1/- each as at December 31, 2005)	2,836	2,520 (@ Rs. 3.60)	2,836	2,100 (@ Rs. 3.00)	2,836	2,520 (@ Rs. 3.60)	2,836	2,100 (@ Rs. 3.00)
Lanka IOC Ltd. (250,000 Ordinary Shares of Rs.10/- each) (250,000 Ordinary Shares of Rs.10/- each as at December 31, 2005)	12,167	7,125 (@ Rs. 28.50)	12,167	8,250 (@ Rs. 33.00)	12,167	7,125 (@ Rs. 28.50)	12,167	8,250 (@ Rs. 33.00)
Vidul Lanka Ltd. (55,000 Ordinary Shares of Rs.10/- each) (50,000 Ordinary Shares of Rs.10/- each as at December 31, 2005)	1,619	1,155 (@ Rs. 21.00)	1,519	1,063 (@ Rs. 21.25)	1,619	1,155 (@ Rs. 21.00)	1,519	1,063 (@ Rs. 21.25)
John Keells Ltd. (30,300 Ordinary Shares of Rs.10/- each) (30,300 Ordinary Shares of Rs.10/- each as at December 31, 2005)	3,006	2,697 (@ Rs. 89.00)	3,006	2,727 (@ Rs. 90.00)	3,006	2,697 (@ Rs. 89.00)	3,006	2,727 (@ Rs. 90.00)
Asha Central Hospitals Ltd. (75,000 Ordinary Shares of Rs.10/- each) (99,100 Ordinary Shares of Rs.10/- each as at December 31, 2005)	3,037	3,056 (@ Rs. 40.75)	3,660	2,354 (@ Rs. 23.75)	3,037	3,056 (@ Rs. 40.75)	3,660	2,354 (@ Rs. 23.75)

**16. Dealing Securities (Contd.)**

	As at 31.12.06		Bank As at 31.12.05		As at 31.12.06		Group As at 31.12.05	
	Cost	Market Value	Cost	Market Value	Cost	Market Value	Cost	Market Value
	Rs.'000	Rs.'000	Rs.'000	Rs.'000	Rs.'000	Rs.'000	Rs.'000	Rs.'000
Dialog Telekom Ltd. (200,000 Ordinary Shares of Rs.1/- each) (225,000 Ordinary Shares of Rs.1/- each as at December 31, 2005)	5,403	5,300 (@ Rs. 26.50)	3,442	3,713 (@ Rs. 16.50)	5,403	5,300 (@ Rs. 26.50)	3,442	3,713 (@ Rs. 16.50)
John Keells Hotels Ltd. (800,000 Ordinary Shares of Rs.10/- each) (125,000 Ordinary Shares of Rs. 10/- each as at December 31, 2005)	7,090	6,800 (@ Rs. 8.50)	11,242	10,125 (@ Rs. 81.00)	7,090	6,800 (@ Rs. 8.50)	11,242	10,125 (@ Rs. 81.00)
Hayleys MGT Knitting Mills Ltd. (50,000 Ordinary Shares of Rs.10/- each) (2005 - Nil)	2,834	2,663 (@ Rs. 53.25)	-	-	2,834	2,663 (@ Rs. 53.25)	-	-
NDB bank (13,700 Ordinary Shares of Rs.10/- each) (2005 - Nil)	2,446	2,747 (@ Rs. 200.50)	-	-	2,446	2,747 (@ Rs. 200.50)	-	-
Sampath Bank Ltd. (2,500 Ordinary Shares of Rs.10/- each) (2005 - Nil)	233	271 (@ Rs. 108.25)	-	-	233	271 (@ Rs. 108.25)	-	-
ACL Cables Ltd. (25,000 Ordinary Shares of Rs.10/- each) (2005 - Nil)	5,213	5,319 (@ Rs. 212.75)	-	-	5,213	5,319 (@ Rs. 212.75)	-	-
Pelwatte Sugar Industries Ltd. (75,000 Ordinary Shares of Rs.10/- each) (2005 - Nil)	2,312	2,644 (@ Rs. 35.25)	-	-	2,312	2,644 (@ Rs. 35.25)	-	-
Hatton National Bank Ltd. (25,000 Ordinary Shares of Rs.10/- each as at December 31, 2005)	-	-	2,050	2,813 (@ Rs. 112.50)	-	-	2,050	2,813 (@ Rs. 112.50)
Hayleys Ltd. (65,000 Ordinary Shares of Rs.10/- each as at December 31, 2005)	-	-	7,157	6,305 (@ Rs. 97.00)	-	-	7,157	6,305 (@ Rs. 97.00)
Distilleries Company of Sri Lanka Ltd. (100,000 Ordinary Shares of Rs.1/- each as at December 31, 2005)	-	-	3,952	3,500 (@ Rs. 35.00)	-	-	3,952	3,500 (@ Rs. 35.00)
Colombo Dockyard Ltd. (149,400 Ordinary Shares of Rs.10/- each as at December 31, 2005)	-	-	4,470	3,324 (@ Rs. 22.25)	-	-	4,470	3,324 (@ Rs. 22.25)
Confifi Hotel Holdings Ltd. (59,600 Ordinary Shares of Rs.10/- each as at December 31, 2005)	-	-	3,927	2,712 (@ Rs. 45.50)	-	-	3,927	2,712 (@ Rs. 45.50)
Riverina Hotels Ltd. (51,500 Ordinary Shares of Rs.10/- each as at December 31, 2005)	-	-	2,327	1,120 (@ Rs. 21.75)	-	-	2,327	1,120 (@ Rs. 21.75)
Sri Lanka Telecom Ltd. (325,000 Ordinary Shares of Rs.10/- each as at December 31, 2005)	-	-	6,418	5,363 (@ Rs. 16.50)	-	-	6,418	5,363 (@ Rs. 16.50)

	As at 31.12.06		Bank		As at 31.12.05		Group	
	Cost	Market Value	Cost	Market Value	Cost	Market Value	Cost	Market Value
	Rs.'000	Rs.'000	Rs.'000	Rs.'000	Rs.'000	Rs.'000	Rs.'000	Rs.'000
Mercantile Leasing Ltd. (100,000 Ordinary Shares of Rs.10/- each as at December 31, 2005)	-	-	5,264	5,200	-	-	5,264	5,200
				(@ Rs. 52.00)				(@ Rs. 52.00)
Asiri Medical Services Ltd. (2,000,000 Ordinary Shares of Rs.1/- each as at December 31, 2005)	-	-	6,914	6,000	-	-	6,914	6,000
				(@ Rs. 3.00)				(@ Rs. 3.00)
Lanka Walltiles Ltd. (312,500 Ordinary Shares of Rs.10/- each as at December 31, 2005)	-	-	13,978	10,234	-	-	13,978	10,234
				(@ Rs. 32.75)				(@ Rs. 32.75)
Kelani Cables Ltd. (46,700 Ordinary Shares of Rs.10/- each as at December 31, 2005)	-	-	2,821	3,257	-	-	2,821	3,257
				(@ Rs. 69.75)				(@ Rs. 69.75)
	<b>162,139</b>	<b>144,896</b>	225,487	182,243	<b>162,139</b>	<b>144,896</b>	225,487	182,243
Provision for diminution in value	(17,243)		(43,244)		(17,243)		(43,244)	
Total	<b>144,896</b>		182,243		<b>144,896</b>		182,243	

### 17. Investments held for Sale

	Holding (%)	As at 31.12.06		Bank		As at 31.12.05		Group	
		Balance	Market Value/ Directors' Valuation	Balance	Market Value/ Directors' Valuation	Balance	Market Value/ Directors' Valuation	Balance	Market Value/ Directors' Valuation
		Rs.'000	Rs.'000	Rs.'000	Rs.'000	Rs.'000	Rs.'000	Rs.'000	Rs.'000
<b>Quoted</b>									
Commercial Leasing Co. Ltd. (Incorporated in Sri Lanka) (5,293,749 Ordinary Shares of Rs.10/- each fully paid)	30.0	86,550	688,187	-	-	260,704	688,187	-	-
			(@ Rs. 130.00)				(@ Rs. 130.00)		
<b>Unquoted</b>									
Commercial Fund Management (Pvt.) Ltd.* (Incorporated in Sri Lanka) (125,000 Ordinary Shares of Rs.100/- each fully paid)	50.0	12,500	21,213	-	-	21,213	21,213	-	-
<b>Units</b>									
Comtrust Equity Fund (11,420,324 Units of Rs. 10.00 each)		119,342	144,353	-	-	119,342	144,353	-	-
			(@ Rs. 12.64)				(@ Rs. 12.64)		
Total		<b>218,392</b>	<b>853,753</b>	-	-	<b>401,259</b>	<b>853,753</b>	-	-

\*Since disposed

**18. Investments held to Maturity**

	<b>Bank</b>				<b>Group</b>			
	<b>As at 31.12.06</b>		<b>As at 31.12.05</b>		<b>As at 31.12.06</b>		<b>As at 31.12.05</b>	
	<b>Cost</b>	<b>Market Value/ Manager's Buying Price</b>						
<b>Rs.'000</b>	<b>Rs.'000</b>	<b>Rs.'000</b>	<b>Rs.'000</b>	<b>Rs.'000</b>	<b>Rs.'000</b>	<b>Rs.'000</b>	<b>Rs.'000</b>	<b>Rs.'000</b>
<b>Quoted SHARES</b>								
Hatton National Bank Ltd. (3,850 Ordinary Shares of Rs. 10/- each) (3,850 Ordinary Shares of Rs. 10/- each as at December 31, 2005)	<b>315</b>	<b>600</b> (@ Rs. 155.75)	315	433 (@ Rs. 112.50)	<b>315</b>	<b>600</b> (@ Rs. 155.75)	315	433 (@ Rs. 112.50)
Sampath Bank Ltd. (1,554 Ordinary Shares of Rs. 10/- each) (1,554 Ordinary Shares of Rs. 10/- each as at December 31, 2005)	<b>72</b>	<b>168</b> (@ Rs. 108.25)	72	140 (@ Rs. 90.00)	<b>72</b>	<b>168</b> (@ Rs. 108.25)	72	140 (@ Rs. 90.00)
Seylan Bank Ltd. (1,000 Ordinary Shares of Rs. 10/- each) (1,000 Ordinary Shares of Rs. 10/- each as at December 31, 2005)	<b>24</b>	<b>35</b> (@ Rs. 35.00)	24	37 (@ Rs. 36.75)	<b>24</b>	<b>35</b> (@ Rs. 35.00)	24	37 (@ Rs. 36.75)
DFCC Bank (1,167 Ordinary Shares of Rs. 10/- each) (7,770,278 Ordinary Shares of Rs. 10/- each as at December 31, 2005)	<b>115</b>	<b>209</b> (@ Rs. 179.50)	1,146,107	1,709,461 (@ Rs. 220.00)	<b>115</b>	<b>209</b> (@ Rs. 179.50)	1,146,107	1,709,461 (@ Rs. 220.00)
Nations Trust Bank Ltd. (1,000 Ordinary Shares of Rs. 10/- each) (1,000 Ordinary Shares of Rs. 10/- each as at December 31, 2005)	<b>14</b>	<b>28</b> (@ Rs. 28.25)	14	24 (@ Rs. 23.50)	<b>14</b>	<b>28</b> (@ Rs. 28.25)	14	24 (@ Rs. 23.50)
NDB bank (2,712 Ordinary Shares of Rs. 10/- each) (1,808 Ordinary Shares of Rs. 10/- each as at December 31, 2005)	<b>215</b>	<b>544</b> (@ Rs. 200.50)	215	380 (@ Rs. 210.00)	<b>215</b>	<b>544</b> (@ Rs. 200.50)	215	380 (@ Rs. 210.00)
<b>DEBENTURES</b>								
Hatton National Bank Ltd. (12%-17% - 2007) (60,000 Debentures of Rs.100/- each) (60,000 Debentures of Rs.100/- each as at December 31, 2005)	<b>6,000</b>	<b>6,015</b> (@ Rs. 100.25)	6,000	6,015 (@ Rs. 100.25)	<b>6,000</b>	<b>6,015</b> (@ Rs. 100.25)	6,000	6,015 (@ Rs. 100.25)
Hatton National Bank Ltd. (10% - 2008) (100,000 Debentures of Rs.100/- each) (100,000 Debentures of Rs.100/- each as at December 31, 2005)	<b>10,000</b>	<b>9,225</b> (@ Rs. 92.25)	10,000	9,225 (@ Rs. 92.25)	<b>10,000</b>	<b>9,225</b> (@ Rs. 92.25)	10,000	9,225 (@ Rs. 92.25)
Sampath Bank Ltd. (Floating rate - 2009) (70,000 Debentures of Rs.100/- each) (70,000 Debentures of Rs.100/- each as at December 31, 2005)	<b>7,000</b>	<b>6,965</b> (@ Rs. 99.50)	7,000	6,965 (@ Rs. 99.50)	<b>7,000</b>	<b>6,965</b> (@ Rs. 99.50)	7,000	6,965 (@ Rs. 99.50)
Senkadagala Finance Ltd. (9% - 2009) (100,000 Debentures of Rs. 100/- each) (100,000 Debentures of Rs. 100/- each as at December 31, 2005)	<b>10,000</b>	<b>10,000</b> (@ Rs. 100.00)	10,000	10,000 (@ Rs. 100.00)	<b>10,000</b>	<b>10,000</b> (@ Rs. 100.00)	10,000	10,000 (@ Rs. 100.00)
DFCC Bank Ltd. (Floating rate - 2011) (10,000 Debentures of Rs. 1,000/- each) (2005 - Nil.)	<b>10,000</b>	<b>10,000</b> (@ Rs. 1,000.00)	-	-	<b>10,000</b>	<b>10,000</b> (@ Rs. 1,000.00)	-	-
	<b>43,755</b>	<b>43,789</b>	1,179,747	1,742,680	<b>43,755</b>	<b>43,789</b>	1,179,747	1,742,680

	Bank				Group			
	As at 31.12.06		As at 31.12.05		As at 31.12.06		As at 31.12.05	
	Cost Rs.'000	Market Value/ Manager's Buying Price Rs.'000	Cost Rs.'000	Market Value/ Manager's Buying Price Rs.'000	Cost Rs.'000	Market Value/ Manager's Buying Price Rs.'000	Cost Rs.'000	Market Value/ Manager's Buying Price Rs.'000
<b>Unquoted</b>								
<b>SHARES</b>								
Credit Information Bureau of Sri Lanka (4,400 Ordinary Shares of Rs. 100/- each) (4,400 Ordinary Shares of Rs. 100/- each as at December 31, 2005)	440	440 (@ Rs. 100.00)	440	440 (@ Rs. 100.00)	440	440 (@ Rs. 100.00)	440	440 (@ Rs. 100.00)
Fitch Ratings Lanka Ltd. (62,500 Ordinary Shares of Rs. 10/- each) (62,500 Ordinary Shares of Rs. 10/- each as at December 31, 2005)	625	625 (@ Rs. 10.00)	625	625 (@ Rs. 10.00)	625	625 (@ Rs. 10.00)	625	625 (@ Rs. 10.00)
Lanka Clear (Pvt) Ltd. (1,000,000 Ordinary Shares of Rs.10/- each) (1,000,000 Ordinary Shares of Rs.10/- each as at December 31, 2005)	10,000	10,000 (@ Rs. 10.00)	10,000	10,000 (@ Rs. 10.00)	10,000	10,000 (@ Rs. 10.00)	10,000	10,000 (@ Rs. 10.00)
Central Depository of Bangladesh Ltd. (6 shares of Bangladesh Taka 1.000 Million each. Converted at Rs. 1.68505 per Taka) (6 shares of Bangladesh Taka 1.000 Million each. Converted at Rs. 1.68505 per Taka as at December 31, 2005)	10,110	10,110	10,110	10,110	10,110	10,110	10,110	10,110
Commercial Insurance Brokers (Pvt) Ltd. (120,000 Ordinary Shares of Rs. 10/- each) (120,000 Ordinary Shares of Rs. 10/- each as at December 31, 2005)	-	-	-	-	100	1,200 (@ Rs. 10.00)	100	1,200 (@ Rs. 10.00)
<b>Units</b>								
Comtrust Equity Fund (11,333,474 Units of Rs.10/- each ) (22,753,798 Units of Rs.10/- each as at December 31, 2005 )	118,511	143,255 (@ Rs. 12.64)	119,457 *	232,544 (@ Rs. 10.22)	118,511	143,255 (@ Rs. 12.64)	119,457 *	232,544 (@ Rs. 10.22)
<b>LEASE BACKED SECURITIES</b>								
Senkadagala Finance Ltd.	63,636	63,636	107,771	107,771	63,636	63,636	107,771	107,771
Commercial Leasing Co. Ltd.	184,404	184,404	277,841	277,841	184,404	184,404	277,841	277,841
Specialist Gasses (Pvt) Ltd	110,700	110,700	-	-	110,700	110,700	-	-
The Finance Company Ltd.	-	-	14,700	14,700	-	-	14,700	14,700
The Finance Company Ltd.	-	-	37,700	37,700	-	-	37,700	37,700
<b>TRUST CERTIFICATES / BONDS</b>								
People's Leasing Co. Ltd.	376,792	376,792	662,292	662,292	376,792	376,792	662,292	662,292
Commercial Leasing Co. Ltd.	1,800	1,800	45,600	45,600	1,800	1,800	45,600	45,600
Senkadagala Finance Ltd.	132,300	132,300	214,750	214,750	132,300	132,300	214,750	214,750
Lanka Orix Leasing Co. Ltd.	300,000	300,000	300,000	300,000	300,000	300,000	300,000	300,000
Government of Bangladesh Prize Bonds	40,706	40,706	110,339	110,339	40,706	40,706	110,339	110,339
	<b>1,350,024</b>	<b>1,374,768</b>	1,911,625	2,024,712	<b>1,350,124</b>	<b>1,375,968</b>	1,911,725	2,025,912
Total	<b>1,393,779</b>	<b>1,418,557</b>	3,091,372	3,767,392	<b>1,393,879</b>	<b>1,419,757</b>	3,091,472	3,768,592

\* At written down value

**19. Loans & Advances**

	<b>Bank</b>		<b>Group</b>	
	<b>2006</b>	2005	<b>2006</b>	2005
	<b>Rs. '000</b>	Rs. '000	<b>Rs. '000</b>	Rs. '000
<b>19.1 Bills of Exchange</b>				
Export bills	<b>2,311,667</b>	2,384,543	<b>2,311,667</b>	2,384,543
Import bills	<b>1,024,072</b>	465,424	<b>1,024,072</b>	465,424
	<b>3,335,739</b>	2,849,967	<b>3,335,739</b>	2,849,967
Less: Loan loss provision [Note 19.1 (a)]	<b>47,541</b>	59,651	<b>47,541</b>	59,651
Interest in suspense	-	-	-	-
	<b>3,288,198</b>	2,790,316	<b>3,288,198</b>	2,790,316
<b>19.1 (a) Movement in the Provision for Bad &amp; Doubtful Bills of Exchange</b>				
<b>Specific Provisions</b>				
Opening balance	<b>59,651</b>	70,841	<b>59,651</b>	70,841
Amount provided	<b>1,058</b>	979	<b>1,058</b>	979
Amount reversed	<b>(13,168)</b>	(12,169)	<b>(13,168)</b>	(12,169)
Closing balance	<b>47,541</b>	59,651	<b>47,541</b>	59,651
<b>19.2 Loans &amp; Advances</b>				
Sri Lankan rupee and foreign currency loans & advances [Note 19.2 (a)]	<b>143,519,823</b>	114,415,133	<b>143,514,134</b>	114,414,777
Less: Loan loss provision [Note 19.2 (b)]	<b>2,358,738</b>	2,052,792	<b>2,358,738</b>	2,052,792
Interest in suspense [Note 19.2 (c)]	<b>3,435,224</b>	3,478,099	<b>3,435,224</b>	3,478,099
	<b>137,725,861</b>	108,884,242	<b>137,720,172</b>	108,883,886
<b>19.2 (a) Sri Lankan Rupee and Foreign Currency Loans &amp; Advances</b>				
<b>Sri Lankan Rupee Loans &amp; Advances</b>				
Overdrafts	<b>31,027,614</b>	23,648,524	<b>31,027,217</b>	23,648,168
Loans	<b>75,661,833</b>	57,461,354	<b>75,656,541</b>	57,461,354
Packing credit	<b>633,020</b>	556,967	<b>633,020</b>	556,967
Staff loans	<b>2,105,006</b>	1,717,097	<b>2,105,006</b>	1,717,097
Foreclosed properties (Note 19.7)	<b>81,613</b>	95,113	<b>81,613</b>	95,113
Other accounts	<b>2,205,177</b>	2,321,262	<b>2,205,177</b>	2,321,262
	<b>111,714,263</b>	85,800,317	<b>111,708,574</b>	85,799,961
<b>Foreign Currency Loans &amp; Advances</b>				
Overdrafts	<b>5,858,882</b>	5,850,835	<b>5,858,882</b>	5,850,835
Loans	<b>20,534,560</b>	17,539,796	<b>20,534,560</b>	17,539,796
Packing credit	<b>5,153,776</b>	5,020,123	<b>5,153,776</b>	5,020,123
Other accounts	<b>258,342</b>	204,062	<b>258,342</b>	204,062
	<b>31,805,560</b>	28,614,816	<b>31,805,560</b>	28,614,816
Total	<b>143,519,823</b>	114,415,133	<b>143,514,134</b>	114,414,777

	<b>Bank</b>		<b>Group</b>	
	<b>2006</b>	2005	<b>2006</b>	2005
	<b>Rs. '000</b>	Rs. '000	<b>Rs. '000</b>	Rs. '000
<b>19.2 (b) Movement in the Provision for Bad &amp; Doubtful Loans &amp; Advances</b>				
<b>Specific Provisions</b>				
Opening balance	<b>2,003,100</b>	1,892,840	<b>2,003,100</b>	1,892,840
Amount provided	<b>435,911</b>	352,146	<b>435,911</b>	352,146
Exchange rate variance on foreign currency provisions	<b>34,715</b>	(17,878)	<b>34,715</b>	(17,878)
Amount reversed	<b>(305,646)</b>	(224,008)	<b>(305,646)</b>	(224,008)
Closing balance	<b>2,168,080</b>	2,003,100	<b>2,168,080</b>	2,003,100
<b>General Provision</b>				
Opening balance	<b>49,692</b>	23,517	<b>49,692</b>	23,517
Amount provided	<b>139,381</b>	27,705	<b>139,381</b>	27,705
Exchange rate variance on foreign currency provisions	<b>1,585</b>	(1,530)	<b>1,585</b>	(1,530)
Amount made specific	-	-	-	-
Closing balance	<b>190,658</b>	49,692	<b>190,658</b>	49,692
Total provision	<b>2,358,738</b>	2,052,792	<b>2,358,738</b>	2,052,792
<b>19.2 (c) Movement in the Interest in Suspense Account</b>				
Opening balance	<b>3,478,099</b>	3,448,587	<b>3,478,099</b>	3,448,587
Interest suspended during the year	<b>311,541</b>	403,258	<b>311,541</b>	403,258
Amount recovered during the year	<b>(354,416)</b>	(373,746)	<b>(354,416)</b>	(373,746)
Closing balance	<b>3,435,224</b>	3,478,099	<b>3,435,224</b>	3,478,099
<b>19.3 Lease Receivable within one year</b>				
Lease rentals receivable within one year from Balance Sheet date	<b>5,191,030</b>	3,895,832	<b>5,144,738</b>	3,857,388
Less: Unearned lease income	<b>1,446,139</b>	882,662	<b>1,434,751</b>	873,368
VAT recoverable	<b>667,896</b>	500,941	<b>661,784</b>	495,711
Loan loss provision	<b>41,567</b>	28,002	<b>41,595</b>	28,062
	<b>3,035,428</b>	2,484,227	<b>3,006,608</b>	2,460,247
<b>19.4 Lease Receivable from one to five years</b>				
Lease rentals receivable from one to five years from Balance Sheet date	<b>8,895,511</b>	6,281,871	<b>8,802,084</b>	6,200,409
Less: Unearned lease income	<b>1,189,949</b>	818,071	<b>1,176,418</b>	807,061
VAT recoverable	<b>1,151,854</b>	815,746	<b>1,139,667</b>	804,676
Loan loss provision	<b>88,533</b>	51,808	<b>88,505</b>	51,748
	<b>6,465,175</b>	4,596,246	<b>6,397,494</b>	4,536,924

	Bank		Group	
	2006 Rs. '000	2005 Rs. '000	2006 Rs. '000	2005 Rs. '000
<b>19.5 Lease Receivable after five years</b>				
Lease rentals receivable after five years				
from Balance Sheet date	<b>20,805</b>	9,842	<b>20,805</b>	9,842
Less: Unearned lease income	<b>627</b>	522	<b>627</b>	522
VAT recoverable	<b>2,714</b>	1,284	<b>2,714</b>	1,284
Loan loss provision	<b>87</b>	40	<b>87</b>	40
	<b>17,377</b>	7,996	<b>17,377</b>	7,996

**19.5 (a) Movement in the provision for Bad & Doubtful Lease Receivable:**

**Specific Provisions**

Opening balance	<b>44,131</b>	39,485	<b>44,131</b>	39,485
Amount provided	<b>58,778</b>	20,449	<b>58,778</b>	20,449
Amount reversed	<b>(20,686)</b>	(15,803)	<b>(20,686)</b>	(15,803)
Closing balance	<b>82,223</b>	44,131	<b>82,223</b>	44,131

**General Provision**

Opening balance	<b>35,719</b>	27,144	<b>35,719</b>	27,144
Amount provided	<b>12,245</b>	8,575	<b>12,245</b>	8,575
Amount made specific	-	-	-	-
Closing balance	<b>47,964</b>	35,719	<b>47,964</b>	35,719
Total provision	<b>130,187</b>	79,850	<b>130,187</b>	79,850

*The maturity analysis of loans & advances is given in Note 33.*

**19.6 Non-Performing Loans & Advances**

Net exposure on non-performing loans and advances as at December 31, before discounting the value of the securities obtained is given below:

	Bank				Group			
	2006 Rs. '000	%	2005 Rs. '000	%	2006 Rs. '000	%	2005 Rs. '000	%
Bills of Exchange	<b>156,551</b>		97,895		<b>156,551</b>		97,895	
Loans and advances	<b>4,947,800</b>		4,764,943		<b>4,947,800</b>		4,764,943	
Lease receivable	<b>199,973</b>		101,279		<b>199,973</b>		101,279	
Non-performing loans & advances (*)	<b>5,304,324</b>		4,964,117		<b>5,304,324</b>		4,964,117	
Add: Interest receivable								
on loans and advances	<b>2,329,379</b>		2,403,007		<b>2,329,379</b>		2,403,007	
Gross non-performing loans & advances	<b>7,633,703</b>		7,367,124		<b>7,633,703</b>		7,367,124	
Less: Interest in suspense [Note 19.2 (c)]	<b>3,435,224</b>		3,478,099		<b>3,435,224</b>		3,478,099	
Net non-performing loans & advances	<b>4,198,479</b>	<b>2.74</b>	3,889,025	3.22	<b>4,198,479</b>	<b>2.74</b>	3,889,025	3.22
Less: Provision for bad & doubtful debts [Note 19.6 (a)]	<b>2,536,465</b>		2,192,293		<b>2,536,465</b>		2,192,293	
Net exposure	<b>1,662,014</b>	<b>1.10</b>	1,696,732	1.43	<b>1,662,014</b>	<b>1.10</b>	1,696,732	1.43

(\*) *This includes foreclosed properties, the details of which are given in Note 19.7.*

Net exposure of Rs. 1,662.014 million (Rs. 1,696.732 million as at December 31, 2005) is covered by securities valued at Rs. 1,662.014 million (Rs. 1,696.732 million as at December 31, 2005) excluding machinery and stocks.

As per the 'Hair Cut Rule' of the Central Bank of Sri Lanka, the extent up to which securities can be discounted for provisioning purposes is 75% at the time of first provisioning, 60% for non-performing loans & advances between 1-2 years in the loss category, 50% for those between 2-3 years in the loss category and 40% for those between 3-4 years in the loss category. It will be at the discretion of the management for cases over 4 years in the loss category.

All loans and advances where the recovery of capital or interest is in arrears for over three months have been classified into the non-performing category in accordance with the guidelines issued by the Central Bank of Sri Lanka. The Bank's computer system has been programmed to classify the loans in accordance with these guidelines. In instances where the recovery of capital or interest is in arrears for over three months, interest credited to the Income Statement on such loans and advances for the first three months too is transferred to interest in suspense.

#### 19.6 (a) Provision for Bad & Doubtful Debts - Summary

	Bank		Group	
	2006 Rs.'000	2005 Rs.'000	2006 Rs.'000	2005 Rs.'000
Opening balance	2,192,293	2,053,828	2,192,293	2,053,828
Provision made during the year	647,372	409,853	647,372	409,853
Exchange rate variance on foreign currency provisions	36,300	(19,408)	36,300	(19,408)
Recoveries/Reversals during the year	(339,500)	(251,980)	(339,500)	(251,980)
Closing balance	<u>2,536,465</u>	<u>2,192,293</u>	<u>2,536,465</u>	<u>2,192,293</u>

#### 19.7 Foreclosed Properties

The foreclosed properties included under loans & advances as at December 31, include the following:

	Extent			Bank			
				2006		2005	
	A	R	P	Cost/W.D.V. Rs.'000	Forced Sale Value Rs.'000	Cost/W.D.V. Rs.'000	Forced Sale Value Rs.'000
1. Land and Building at Kochchikade, Negombo (*)	2	2	36.91	81,613	125,000	81,613	125,000
2. Land at Thaladena, Pamunugama	11	1	5.60	-	-	13,500	13,500
Total				<u>81,613</u>	<u>125,000</u>	<u>95,113</u>	<u>138,500</u>

A = Acres, R = Roods, P = Perches

(\*) Bank acquired this hotel property in 1999 in settlement of a debt due to the Bank. With the approval of the Central Bank of Sri Lanka, Bank entered into a management agreement with Serendib Leisure Management (Pvt) Ltd. which expired in December 2002. Currently, this hotel is closed for operations.

### 19.8 Concentration of Credit Risk

Sectorwise analysis of the loans & advances portfolio reflecting the exposure to credit risk in the various sectors is given below:

	Bank				Group			
	2006		2005		2006		2005	
	Rs.'000	%	Rs.'000	%	Rs.'000	%	Rs.'000	%
Exports	16,471,461	10.68	15,848,433	12.99	16,471,461	10.69	15,848,433	13.00
Tourism & allied	5,143,570	3.34	4,226,475	3.46	5,143,570	3.34	4,226,475	3.47
Industrial	24,047,631	15.60	19,517,336	15.99	24,047,631	15.61	19,517,336	16.00
Agriculture & fishing	1,606,924	1.04	1,664,978	1.36	1,606,924	1.04	1,664,978	1.37
Commercial trading	8,561,694	5.55	8,930,045	7.32	8,561,694	5.56	8,930,045	7.32
Imports	20,206,052	13.11	17,645,871	14.46	20,206,052	13.11	17,645,871	14.47
Consumption	5,840,736	3.79	4,491,896	3.68	5,840,736	3.79	4,491,896	3.68
Services	19,787,598	12.83	17,394,590	14.25	19,691,095	12.78	17,311,288	14.20
Housing & construction	9,393,570	6.09	7,139,339	5.85	9,393,570	6.10	7,139,339	5.85
Others	43,115,115	27.97	25,171,449	20.64	43,109,426	27.98	25,171,449	20.64
Total loans & advances	154,174,351	100.00	122,030,412	100.00	154,072,159	100.00	121,947,110	100.00

### 20. Investments in Associate Companies

	%	Bank				Group			
		31.12.06		31.12.05		31.12.06		31.12.05	
		Balance	Market Value/ Directors' Valuation	Balance	Market Value/ Directors' Valuation	Balance	Market Value/ Directors' Valuation	Balance	Market Value/ Directors' Valuation
Rs.'000	Rs.'000	Rs.'000	Rs.'000	Rs.'000	Rs.'000	Rs.'000	Rs.'000		
<b>Quoted</b>									
Commercial Leasing Co. Ltd. (Incorporated in Sri Lanka)	30.00								
(3,630,001 Ordinary Shares of Rs. 10/- each fully paid)		50,250	609,538	50,250	618,008	50,250	609,538	50,250	618,008
(3,630,001 Ordinary Shares of Rs. 10/- each fully paid as at December 31, 2005)			(@ Rs. 130.00)		(@ Rs. 170.25)		(@ Rs. 130.00)		(@ Rs. 170.25)
Add: Share Premium held by the Bank						26,146		26,146	
Add: Rights issue of shares (604,999 Ordinary Shares of Rs. 10/- each fully paid)		36,300	78,650	-	-	36,300	78,650	-	-
Add: Share of profit/(loss) applicable to the Bank			(@ Rs. 130.00)			(@ Rs. 130.00)			
Balance at the beginning of the year						148,181		107,972	
Changes in accounting policy for accounting for deferred taxation		-	-	-	-	(41,838)	-	-	-
Current year's share of profit/(loss) after tax						41,665		61,479	
Less: Dividend received during the year						-		(21,270)	
Current year's retained profit/(loss)						41,665		40,209	
		86,550	688,188	50,250	618,008	260,704	688,188	224,577	618,008
Transferred to investments held for sale		(86,550)	(688,188)	-	-	(260,704)	(688,188)	-	-
Balance at the end of the year		-	-	50,250	618,008	-	-	224,577	618,008

	31.12.06		Bank		31.12.06		Group	
	Balance	Market Value/Directors' Valuation	Balance	Market Value/Directors' Valuation	Balance	Market Value/Directors' Valuation	Balance	Market Value/Directors' Valuation
	Rs.'000	Rs.'000	Rs.'000	Rs.'000	Rs.'000	Rs.'000	Rs.'000	Rs.'000
<b>Unquoted</b>								
Commercial Fund Management (Pvt) Ltd. (Incorporated in Sri Lanka) <b>50.00</b> (125,000 Ordinary Shares of Rs. 100/- each fully paid)	<b>12,500</b>	<b>21,213</b>	12,500	18,290	<b>12,500</b>	<b>21,213</b>	12,500	18,290
(125,000 Ordinary Shares of Rs. 100/- each fully paid as at Dec. 31, 2005)								
Add: Share of profit/(loss) applicable to the Bank								
Balance at the beginning of the year					<b>5,790</b>		3,615	
Current year's share of profit/(loss) after tax					<b>3,519</b>		3,384	
Less: Dividend received during the year					<b>(596)</b>		(1,209)	
Current year's retained profit/(loss)					<b>2,923</b>		2,175	
					<b>8,713</b>		5,790	
	<b>12,500</b>	<b>21,213</b>	12,500	18,290	<b>21,213</b>	<b>21,213</b>	18,290	18,290
Transferred to investments held for sale	<b>(12,500)</b>	<b>(21,213)</b>	-	-	<b>(21,213)</b>	<b>(21,213)</b>	-	-
Balance at the end of the year	<b>-</b>	<b>-</b>	12,500	18,290	<b>-</b>	<b>-</b>	18,290	18,290
Equity Investments Lanka Ltd. (Incorporated in Sri Lanka) <b>22.92</b> (4,110,938 Ordinary Shares of Rs. 10/- each fully paid)	<b>44,331</b>	<b>40,965</b>	44,331	39,922	<b>44,331</b>	<b>40,965</b>	44,331	39,922
(4,110,938 Ordinary Shares of Rs.10/- each fully paid as at Dec. 31, 2005)								
Add: Share of profit/(loss) applicable to the Bank								
Balance at the beginning of the year					<b>(4,409)</b>		(3,596)	
Current year's share of profit/(loss) after tax					<b>2,276</b>		1,242	
Less: Dividend received during the year					<b>(1,233)</b>		(2,055)	
Current year's retained profit/(loss)					<b>1,043</b>		(813)	
					<b>(3,366)</b>		(4,409)	
Balance at the end of the year	<b>44,331</b>	<b>40,965</b>	44,331	39,922	<b>40,965</b>	<b>40,965</b>	39,922	39,922
Total Value of Investments in Quoted & Unquoted Associate Companies	<b>44,331</b>		107,081		<b>40,965</b>		282,789	
Total Market Value/Directors' Valuation of Investments in Associate Companies		<b>40,965</b>		676,220		<b>40,965</b>		676,220

## 21. Investments in Subsidiary Companies

	% Holding	31.12.06		Bank 31.12.05		31.12.06		Group 31.12.05	
		Balance	Market Value/ Directors' Valuation	Balance	Market Value/ Directors' Valuation	Balance	Market Value/ Directors' Valuation	Balance	Market Value/ Directors' Valuation
		Rs.'000	Rs.'000	Rs.'000	Rs.'000	Rs.'000	Rs.'000	Rs.'000	Rs.'000
<b>Quoted</b>									
Commercial Development Co. Ltd. (Incorporated in Sri Lanka)	94.55								
(11,345,705 Ordinary Shares of Rs.10/- each fully paid)		274,393	737,471	274,393	624,014	-	-	-	-
(11,345,705 Ordinary Shares of Rs. 10/- each fully paid as at December 31, 2005)			(@ Rs. 65.00)		(@ Rs. 55.00)				
<b>Unquoted</b>									
Commercial Bank Primary Dealer Ltd. (Incorporated in Sri Lanka)	100.00								
(15,000,000 Ordinary Shares of Rs.10/- each fully paid)		150,000	150,000	150,000	150,000	-	-	-	-
(15,000,000 Ordinary Shares of Rs. 10/- each fully paid as at December 31, 2005)			(@ Rs. 10.00)		(@ Rs. 10.00)				
ONEzero Company Ltd. (Incorporated in Sri Lanka)	100.00								
(500,000 Ordinary Shares of Rs.10/- each fully paid)		5,000	5,000	5,000	5,000	-	-	-	-
(500,000 Ordinary Shares of Rs. 10/- each fully paid as at December 31, 2005)			(@ Rs. 10.00)		(@ Rs. 10.00)				
X-pertise Ltd. (Incorporated in Sri Lanka)	100.00								
(428,797 Ordinary Shares of Rs. 10/- each fully paid)		4,288	4,288	4,288	4,288	-	-	-	-
(428,797 Ordinary Shares of Rs. 10/- each fully paid as at December 31, 2005)			(@ Rs. 10.00)		(@ Rs. 10.00)				
		<b>433,681</b>	<b>896,759</b>	433,681	783,302	-	-	-	-

## 22. Other Assets

	Bank		Group	
	2006 Rs.'000	2005 Rs.'000	2006 Rs.'000	2005 Rs.'000
Deposits & prepayments	190,266	198,796	195,590	206,909
Clearing account balance	1,870,827	777,958	1,870,827	777,958
Other accounts	734,924	2,015,037	776,565	1,934,912
	<b>2,796,017</b>	<b>2,991,791</b>	<b>2,842,982</b>	<b>2,919,779</b>

**23. Property, Plant & Equipment**

	Freehold Land	Freehold Buildings	Leasehold Buildings	Computer Equipment	Motor Vehicles	Office Equipment & Furniture	Capital Work-in- Progress	<b>31.12.06 Total</b>	31.12.05 Total
	Rs.'000	Rs.'000	Rs.'000	Rs.'000	Rs.'000	Rs.'000	Rs.'000	<b>Rs.'000</b>	Rs.'000
<b>Bank</b>									
Cost/Valuation									
as at beginning of the year	1,050,415	881,817	97,610	1,552,921	37,354	1,164,747	1,673	<b>4,786,537</b>	4,190,937
Additions for the year	11,398	18,096	905	176,279	14,686	235,294	21,513	<b>478,171</b>	648,630
Disposals during the year	-	-	-	(59,996)	(5,527)	(8,661)	-	<b>(74,184)</b>	(46,654)
Transfers/Adjustments	-	-	-	701	-	(443)	-	<b>258</b>	(6,376)
As at end of the year	<u>1,061,813</u>	<u>899,913</u>	<u>98,515</u>	<u>1,669,905</u>	<u>46,513</u>	<u>1,390,937</u>	<u>23,186</u>	<b><u>5,190,782</u></b>	<u>4,786,537</u>
Accumulated depreciation/ amortisation									
as at beginning of the year	-	39,553	3,142	950,827	33,944	726,709	-	<b>1,754,175</b>	1,523,323
Charge for the year	-	35,232	3,175	156,615	3,155	91,954	-	<b>290,131</b>	260,885
Disposals during the year	-	-	-	(58,481)	(5,527)	(7,014)	-	<b>(71,022)</b>	(29,812)
Transfers/Adjustments	-	-	-	551	-	(315)	-	<b>236</b>	(221)
As at end of the year	<u>-</u>	<u>74,785</u>	<u>6,317</u>	<u>1,049,512</u>	<u>31,572</u>	<u>811,334</u>	<u>-</u>	<b><u>1,973,520</u></b>	<u>1,754,175</u>
<b>Net Book Value as at 31.12.06</b>	<b><u>1,061,813</u></b>	<b><u>825,128</u></b>	<b><u>92,198</u></b>	<b><u>620,393</u></b>	<b><u>14,941</u></b>	<b><u>579,603</u></b>	<b><u>23,186</u></b>	<b><u>3,217,262</u></b>	
Net Book Value as at 31.12.05	<u>1,050,415</u>	<u>842,264</u>	<u>94,468</u>	<u>602,094</u>	<u>3,410</u>	<u>438,038</u>	<u>1,673</u>		<u>3,032,362</u>
<b>Group</b>									
Cost / Valuation									
as at beginning of the year	1,050,415	881,817	274,247	1,553,783	142,003	1,212,350	1,673	<b>5,116,288</b>	4,492,307
Additions for the year	11,398	18,096	905	176,806	55,878	237,246	27,126	<b>527,455</b>	685,327
Disposals during the year	-	-	-	(59,996)	(17,047)	(8,661)	-	<b>(85,704)</b>	(54,970)
Transfers/Adjustments	-	-	-	632	-	(375)	-	<b>257</b>	(6,376)
As at end of the year	<u>1,061,813</u>	<u>899,913</u>	<u>275,152</u>	<u>1,671,225</u>	<u>180,834</u>	<u>1,440,560</u>	<u>28,799</u>	<b><u>5,558,296</u></b>	<u>5,116,288</u>
Accumulated depreciation/ amortisation									
as at beginning of the year	-	39,553	55,313	951,263	74,414	757,706	-	<b>1,878,249</b>	1,625,151
Charge for the year	-	35,232	7,591	156,761	29,343	94,797	-	<b>323,724</b>	290,076
Disposals during the year	-	-	-	(58,481)	(15,925)	(7,014)	-	<b>(81,420)</b>	(36,757)
Transfers/Adjustments	-	-	-	536	-	(315)	-	<b>221</b>	(221)
As at end of the year	<u>-</u>	<u>74,785</u>	<u>62,904</u>	<u>1,050,079</u>	<u>87,832</u>	<u>845,174</u>	<u>-</u>	<b><u>2,120,774</u></b>	<u>1,878,249</u>
<b>Net Book Value as at 31.12.06</b>	<b><u>1,061,813</u></b>	<b><u>825,128</u></b>	<b><u>212,248</u></b>	<b><u>621,146</u></b>	<b><u>93,002</u></b>	<b><u>595,386</u></b>	<b><u>28,799</u></b>	<b><u>3,437,522</u></b>	
Net Book Value as at 31.12.05	<u>1,050,415</u>	<u>842,264</u>	<u>218,934</u>	<u>602,520</u>	<u>67,589</u>	<u>454,644</u>	<u>1,673</u>		<u>3,238,039</u>

With the permission of the Monetary Board of the Central Bank of Sri Lanka, freehold and leasehold land & buildings of the Bank were revalued by professionally qualified independent valuers as at December 31, 2004. The surplus on the revaluation amounting to Rs. 1,131.147 million was credited to the Revaluation Reserve Account.

The carrying amount of these freehold land & buildings if they were carried at cost less accumulated depreciation is as follows:

	2006			2005		
	Cost	Accumulated Depreciation	Net Book Value	Cost	Accumulated Depreciation	Net Book Value
	Rs.'000	Rs.'000	Rs.'000	Rs.'000	Rs.'000	Rs.'000
Land	<u>299,710</u>	<u>-</u>	<u>299,710</u>	<u>288,312</u>	<u>-</u>	<u>288,312</u>
Buildings	<u>586,084</u>	<u>141,538</u>	<u>444,546</u>	<u>567,988</u>	<u>125,475</u>	<u>442,513</u>
Total	<u><b>885,794</b></u>	<u><b>141,538</b></u>	<u><b>744,256</b></u>	<u><b>856,300</b></u>	<u><b>125,475</b></u>	<u><b>730,825</b></u>

There were no significant changes in the Bank's or Group's Property, Plant & Equipment during the year, other than the following:

**Bank**

Transfer of leasehold land of Rs. 84.804 million to other assets in accordance with the Sri Lanka Accounting Standard No. 19 (Revised 2005) - Leases.

**Group**

Transfer of leasehold land of Rs. 43.860 million of Commercial Development Company Ltd., to other assets in accordance with the Sri Lanka Accounting Standard No. 19 (Revised 2005) - Leases.

**24. Intangible Assets**

	Bank		Group	
	2006 Rs. '000	2005 Rs. '000	2006 Rs. '000	2005 Rs. '000
Cost/Valuation as at beginning of the year	429,230	385,123	430,360	385,123
Additions for the year	96,657	44,107	97,657	45,237
Disposals during the year	-	-	-	-
Transfers/Adjustments	-	-	(650)	-
As at end of the year	525,887	429,230	527,367	430,360
Accumulated amortisation as at beginning of the year	279,245	241,905	279,245	241,905
Amortisation for the year	85,648	37,340	85,889	37,340
Disposals during the year	-	-	-	-
Transfers/Adjustments	(535)	-	(535)	-
As at end of the year	364,358	279,245	364,599	279,245
<b>Net Book Value</b>	<b>161,529</b>	<b>149,985</b>	<b>162,768</b>	<b>151,115</b>

**25. Deposits from Customers**

**Local Currency Deposits**

Current account deposits	14,305,620	12,376,704	14,203,723	12,266,491
Savings deposits	42,952,361	35,203,524	42,952,016	35,203,170
Time deposits	48,060,083	34,472,553	48,060,083	34,472,553
Certificates of deposit	3,302,756	3,298,219	3,302,756	3,298,219
	<b>108,620,820</b>	<b>85,351,000</b>	<b>108,518,578</b>	<b>85,240,433</b>

**Foreign Currency Deposits**

Current account deposits	4,575,136	3,403,137	4,575,136	3,403,137
Savings deposits	21,380,050	16,076,665	21,380,050	16,076,665
Time deposits	23,058,064	22,770,478	23,058,064	22,770,478
	<b>49,013,250</b>	<b>42,250,280</b>	<b>49,013,250</b>	<b>42,250,280</b>
Total deposits	<b>157,634,070</b>	<b>127,601,280</b>	<b>157,531,828</b>	<b>127,490,713</b>

**25 (a) Analysis of Deposits**

Deposits from banks	145,316	1,469,362	145,316	1,469,362
Deposits from finance companies	1,364,365	1,008,413	1,364,365	1,008,413
Deposits from other customers	156,124,389	125,123,505	156,022,147	125,012,938
	<b>157,634,070</b>	<b>127,601,280</b>	<b>157,531,828</b>	<b>127,490,713</b>

The maturity analysis of deposits is given in Note 33.

	Bank		Group	
	2006 Rs.'000	2005 Rs.'000	2006 Rs.'000	2005 Rs.'000
<b>26. Borrowings</b>				
Call money borrowings	1,800,000	721,414	1,800,000	721,414
Borrowings from banks abroad	10,973,127	9,236,024	10,973,127	9,236,024
Refinance borrowings	5,095,989	3,429,624	5,095,989	3,429,624
Long-term borrowings	1,075,000	–	1,075,000	–
	<b>18,944,116</b>	<b>13,387,062</b>	<b>18,944,116</b>	<b>13,387,062</b>

**27. Other Liabilities**

Accrued expenditure and interest	3,659,974	2,857,936	3,662,898	2,859,052
Cheques sent on clearing	2,062,161	2,428,802	2,062,161	2,428,802
Contribution to the restructured Pension Scheme	1,780,495	–	1,780,495	–
Provision for Gratuity	18,095	5,981	23,231	9,712
Other accounts	883,302	823,183	873,258	811,358
	<b>8,404,027</b>	<b>6,115,902</b>	<b>8,402,043</b>	<b>6,108,924</b>

**28. Deferred Taxation**

As at December 31	Bank				Group			
	2006		2005		2006		2005	
	Temporary Difference Rs.'000	Tax Effect Rs.'000	Temporary Difference Rs.'000	Tax Effect Rs.'000	Temporary Difference Rs.'000	Tax Effect Rs.'000	Temporary Difference Rs.'000	Tax Effect Rs.'000
As at beginning of the year	726,658	214,146	794,667	238,400	770,729	227,367	835,973	250,792
Amount originating/(reversing) during the year	940,573	366,389	(68,009)	(24,254)	1,023,376	397,573	(65,244)	(23,425)
As at end of the year	<b>1,667,231</b>	<b>580,535</b>	<b>726,658</b>	<b>214,146</b>	<b>1,794,105</b>	<b>624,940</b>	<b>770,729</b>	<b>227,367</b>

Current year's charge of Deferred Tax of Rs. 366.389 million comprises of provision on brought forward balances of Assets Leased to Customers as mentioned below and the current year's charge/(reversal) on other temporary differences arising on Property, Plant and Equipment, Assets Leased to Customers, General Provision on Loans and Advances and Provision for Gratuity payable.

Tax effect on temporary differences of assets leased to customers is given below:

As at December 31	Bank				Group			
	2006		2005		2006		2005	
	Temporary Difference Rs.'000	Tax Effect Rs.'000	Temporary Difference Rs.'000	Tax Effect Rs.'000	Temporary Difference Rs.'000	Tax Effect Rs.'000	Temporary Difference Rs.'000	Tax Effect Rs.'000
As at beginning of the year	1,020,323	357,113	814,807	244,442	1,020,323	357,113	814,807	244,442
Amount originating/(reversing) during the year	232,433	81,351	205,516	112,671	232,433	81,351	205,516	112,671
As at end of the year	<b>1,252,756</b>	<b>438,464</b>	<b>1,020,323</b>	<b>357,113</b>	<b>1,252,756</b>	<b>438,464</b>	<b>1,020,323</b>	<b>357,113</b>

Deferred Tax of Rs. 357.113 million relates to the temporary differences of the brought forward balances of Assets Leased to Customers which has been adjusted against the Retained Profits brought forward in accordance with the Sri Lanka Accounting Standard No. 14 on Income Taxes.

## 29. Debentures

As at December 31, 2006, debentures consisted of 6,680,440 Unsecured Subordinated Redeemable Debentures of Rs. 1,000/- each issued by the Bank in 2003, 2004, 2005 and 2006.

As at December 31, 2005, debentures consisted of 4,553,410 Unsecured Subordinated Redeemable Debentures of Rs. 1,000/- each issued by the Bank in 2003, 2004, and 2005.

	Bank		Group	
	2006 Rs.'000	2005 Rs.'000	2006 Rs.'000	2005 Rs.'000
As at beginning of the year	4,553,410	3,244,410	4,553,410	3,244,410
Issued during the year	2,127,030	1,309,000	2,127,030	1,309,000
Redeemed during the year	-	-	-	-
As at end of the year	<b>6,680,440</b>	4,553,410	<b>6,680,440</b>	4,553,410

	Colombo Stock Exchange Listing	Interest Payable Frequency	Allotment Date	Maturity Date	Effective Annual Yield		Value as at December 31	
					2006	2005	2006	2005
							Rs. '000	Rs. '000
<b>Debenture Categories</b>								
<b>Fixed Rate</b>								
2003/2008 - 10.00% p.a.	Listed	Quarterly	12.05.2003	12.05.2008	10.38%	10.38%	115,890	115,890
2005/2010 - 12.00% p.a.	Not listed	Annually	10.10.2005	10.10.2010	12.00%	12.00%	284,000	284,000
2006/2011 - 12.00% p.a.	Not listed	Annually	16.05.2006	16.05.2011	12.00%	-	15,000	-
2006/2016 - 13.25% p.a.	Not listed	Annually	16.05.2006	16.05.2016	13.25%	-	505,000	-
2006/2011 - 13.50% p.a.	Listed	Annually	18.12.2006	18.12.2011	13.50%	-	527,800	-
2006/2013 - 13.75% p.a.	Listed	Annually	18.12.2006	18.12.2013	13.75%	-	250	-
2006/2016 - 14.00% p.a.	Listed	Annually	18.12.2006	18.12.2016	14.00%	-	467,260	-
							<b>1,915,200</b>	<b>399,890</b>
<b>Floating Rate</b>								
2003/2008 - 3 months TB rate (Net) + 2% p.a.	Listed	Quarterly	12.05.2003	12.05.2008	12.79%	10.77%	2,128,520	2,128,520
2004/2009 - 3 months TB rate (Net) + 2% p.a.	Not listed	Quarterly	01.10.2004	01.10.2009	12.79%	10.77%	1,000,000	1,000,000
2005/2010 - 3 months TB rate (Net) + 2% p.a.	Not listed	Quarterly	10.10.2005	10.10.2010	12.79%	11.65%	120,000	120,000
2005/2010 - 3 months TB rate (Gross) + 1% p.a.	Not listed	Quarterly	10.10.2005	10.10.2010	12.94%	11.73%	905,000	905,000
2006/2011 - 3 months TB rate (Net) + 2% p.a.	Not listed	Quarterly	16.05.2006	16.05.2011	12.82%	-	15,000	-
2006/2011 - 3 months TB rate (Gross) + 1% p.a.	Not listed	Quarterly	16.05.2006	16.05.2011	12.97%	-	465,000	-
2006/2011 - 12 months TB rate (Gross) + 1% p.a.	Listed	Annually	18.12.2006	18.12.2011	15.19%	-	131,020	-
2006/2013 - 12 months TB rate (Gross) + 1% p.a.	Listed	Annually	18.12.2006	18.12.2013	15.19%	-	300	-
2006/2016 - 12 months TB rate (Gross) + 1% p.a.	Listed	Annually	18.12.2006	18.12.2016	15.19%	-	400	-
							<b>4,765,240</b>	<b>4,153,520</b>
Total debentures as at end of the year							<b>6,680,440</b>	<b>4,553,410</b>

3 months TB rate (Gross) - three months Treasury Bill rate before 10% Withholding Tax rate as published by the Central Bank of Sri Lanka immediately prior to the commencement of each interest period.

3 months TB rate (Net) - three months Treasury Bill rate after 10% Withholding Tax rate as published by the Central Bank of Sri Lanka immediately prior to the commencement of each interest period.

12 months TB rate (Gross) - twelve months Treasury Bill rate before 10% Withholding Tax rate as published by the Central Bank of Sri Lanka immediately prior to the commencement of each interest period.

**30. Share Capital**

	<b>Bank</b>		<b>Group</b>	
	<b>2006</b>	2005	<b>2006</b>	2005
	<b>Rs.'000</b>	Rs.'000	<b>Rs.'000</b>	Rs.'000
<b>Authorised</b>				
250,000,000 Ordinary Voting Shares of Rs. 10/- each	<b>2,500,000</b>	2,500,000	<b>2,500,000</b>	2,500,000
50,000,000 Ordinary Non-Voting Shares of Rs. 10/- each	<b>500,000</b>	500,000	<b>500,000</b>	500,000
200,000,000 Cumulative Redeemable Preference Shares of Rs. 10/- each	<b>2,000,000</b>	2,000,000	<b>2,000,000</b>	2,000,000
	<b>5,000,000</b>	5,000,000	<b>5,000,000</b>	5,000,000
<b>Issued &amp; Fully Paid</b>				
<b>Ordinary Shares - Voting</b>				
Opening balance - 132,780,522 shares of Rs. 10/- each (65,029,769 shares in 2005 )	<b>1,327,806</b>	650,298	<b>1,327,806</b>	650,298
Issue of 1,361,591 shares of Rs. 10/- each under Employee Share Option Plan	-	13,616	-	13,616
Bonus Issue of 66,389,162 shares of Rs. 10/- each	-	663,892	-	663,892
Issue of 737,742 Shares of Rs. 10/- each under Employee Share Option Plan	<b>7,377</b>	-	<b>7,377</b>	-
Closing balance - 133,518,264 shares of Rs. 10/- each (132,780,522 shares in 2005)	<b>1,335,183</b>	1,327,806	<b>1,335,183</b>	1,327,806
<b>Ordinary Shares - Non-Voting</b>				
Opening balance - 9,300,460 shares of Rs. 10/- each (4,650,230 shares in 2005)	<b>93,003</b>	46,501	<b>93,003</b>	46,501
Bonus Issue of 4,650,230 shares of Rs. 10/- each	-	46,502	-	46,502
Closing balance - 9,300,460 shares of Rs. 10/- each (9,300,460 shares in 2005)	<b>93,003</b>	93,003	<b>93,003</b>	93,003
<b>13% Cumulative Redeemable Preference Shares</b>				
Opening balance - 90,655,500 shares of Rs. 10/- each (90,655,500 Shares in 2005)	<b>906,555</b>	906,555	<b>906,555</b>	906,555
Redemption of shares during the year	<b>(906,555)</b>	-	<b>(906,555)</b>	-
Closing balance - Nil (90,655,500 Shares in 2005)	-	906,555	-	906,555
<b>11.25% Cumulative Redeemable Preference Shares</b>				
Opening balance - 100,000,000 shares of Rs. 10/- each	<b>1,000,000</b>	1,000,000	<b>1,000,000</b>	1,000,000
Redemption of shares during the year	-	-	-	-
Closing balance - 100,000,000 shares of Rs. 10/- each	<b>1,000,000</b>	1,000,000	<b>1,000,000</b>	1,000,000
Total	<b>2,428,186</b>	3,327,364	<b>2,428,186</b>	3,327,364

These shares are quoted in the Colombo Stock Exchange.

Rs. 906.555 million worth 13% Cumulative Redeemable Preference Shares were allotted on September 21, 2001 and were redeemed on September 20, 2006. An equivalent amount was transferred to the Capital Redemption Reserve Fund out of the Post Tax Profits.

The 11.25% Cumulative Redeemable Preference Shares were allotted on May 13, 2003 and will be redeemed on May 12, 2008. Bank intends to build up a Capital Redemption Reserve Fund out of the profits otherwise available for dividends on redemption of these Preference Shares.

**Employee Share Option Plan**

The Bank obtained the approval of the shareholders at an Extraordinary General Meeting held in September 2002, to introduce an Employee Share Option Plan for the benefit of all the executive officers in Grade III and above by creating up to 5% of the ordinary voting shares at the rate of 1.25% shares each year over a period of four years, upon the Bank achieving specified performance targets.

The details relating to the four tranches of the Employee Share Option Plan are given below:

Tranche	No. of Options (*)	Date given	Price (Rs.) (**)	Exercisable between	Exercised as at end of the year
I	650,000	March 31, 2003	147.84	April 01, 2004 to March 31, 2008	624,857
II	812,500	March 31, 2004	168.00	April 01, 2005 to March 31, 2009	774,674
III	1,637,947	March 31, 2005	163.00	April 01, 2006 to March 31, 2010	729,485
IV	1,659,756	March 31, 2006	161.74	April 01, 2007 to March 31, 2011	–
	4,760,203				2,129,016

(\*) Giving options under each tranche is based on the overall performance of the Bank for each year.

(\*\*) Determined on the basis of the weighted average price of the voting shares of the Bank between October 1 and December 31 of each year, for which options are given to eligible employees.

The number of options given to the Managing Director under tranches I, II, III & IV are 25,623, 30,753, 63,349 and 58,963 respectively.

### 31. Statutory Reserve Fund

	Bank		Group	
	2006 Rs.'000	2005 Rs.'000	2006 Rs.'000	2005 Rs.'000
Opening balance	1,421,000	1,009,000	1,421,819	1,009,819
Add: Transfer during the year	7,500	412,000	7,500	412,000
Closing balance	1,428,500	1,421,000	1,429,319	1,421,819

The balance in the Statutory Reserve Fund account will be used only for the purposes specified in the Section 20 (2) of the Banking Act No. 30 of 1988.

### 32. Reserves

	Bank		Group	
	2006 Rs.'000	2005 Rs.'000	2006 Rs.'000	2005 Rs.'000
<b>Capital Reserves</b>				
Share Premium Account [Refer Note 32 (a)]	1,728,793	1,679,604	1,728,793	1,679,604
Revaluation Reserve [Refer Notes 23 and 32 (b)]	1,288,177	1,288,177	1,288,177	1,288,177
	3,016,970	2,967,781	3,016,970	2,967,781
<b>Revenue Reserves</b>				
General Reserve [Refer Note 32 (c)]	7,978,158	7,625,000	7,978,158	7,625,000
Capital Redemption Reserve Fund [Refer Note 32 (d)]	906,555	–	906,555	–
Foreign Currency Translation Reserve [Refer Note 32 (e)]	(416,049)	–	(416,049)	–
Unappropriated profit/(loss) carried forward [Refer Note 12]	500,521	427,238	673,321	611,609
	8,969,185	8,052,238	9,141,985	8,236,609
Total	11,986,155	11,020,019	12,158,955	11,204,390

**32 (a) Share Premium Account**

	Bank		Group	
	2006 Rs.'000	2005 Rs.'000	2006 Rs.'000	2005 Rs.'000
Opening balance	1,679,604	2,186,874	1,679,604	2,186,874
Proceeds from issue of shares under Employee Share Option Plan	52,686	203,124	52,686	203,124
Utilised for the bonus issue of shares	-	(710,394)	-	(710,394)
Writing-off of debenture issue expenses	(3,497)	-	(3,497)	-
Closing balance	<u>1,728,793</u>	<u>1,679,604</u>	<u>1,728,793</u>	<u>1,679,604</u>

Share Premium account is generally used for bonus issue of ordinary shares and writing-off of share and debenture issue expenses as per Section 58 (2) of the Companies Act No. 17 of 1982.

**32 (b) Revaluation Reserve**

The Revaluation Reserve relates to revaluation of Land & Buildings and represents the increase in the fair value of the Land & Buildings as at December 31, 2004, the date of revaluation.

The Licensed Commercial Banks are allowed to carry out revaluation of their Land & Buildings every seven years and treat 50% of the surplus as supplementary capital in the Tier II of their Capital Base in the computation of Risk-Weighted Capital Adequacy Ratio.

**32 (c) General Reserve**

	Bank		Group	
	2006 Rs.'000	2005 Rs.'000	2006 Rs.'000	2005 Rs.'000
Opening balance	7,625,000	6,545,000	7,625,000	6,545,000
Transfer to Foreign Currency Translation Reserve due to changes in accounting policy	404,375	-	404,375	-
Prior year adjustment for Deferred Tax on Leased Assets	(357,113)	-	(357,113)	-
Appreciation in the value of investment in Comtrust Equity Fund	118,396	-	118,396	-
Transfer from the Income Statement	187,500	1,080,000	187,500	1,080,000
Closing balance	<u>7,978,158</u>	<u>7,625,000</u>	<u>7,978,158</u>	<u>7,625,000</u>

This comprises amounts appropriated by the Board of Directors for the general banking reserve.

**32 (d) Capital Redemption Reserve Fund**

Opening balance	-	-	-	-
Add: Transfer from Income Statement	906,555	-	906,555	-
Closing balance	<u>906,555</u>	<u>-</u>	<u>906,555</u>	<u>-</u>

This represents the nominal value of preference shares redeemed out of profits. The balance in this account can be used only for the purposes specified in Section 57 (5) of the Companies Act No. 17 of 1982.

**32 (e) Foreign Currency Translation Reserve**

Opening balance	-	-	-	-
Transfer due to changes in accounting policy	(404,375)	-	(404,375)	-
Net unrealised gains/(losses) for the year from the translation of Bangladesh operations	(11,674)	-	(11,674)	-
Closing balance	<u>(416,049)</u>	<u>-</u>	<u>(416,049)</u>	<u>-</u>

This represents the gain/(loss) on translation of the Financial Statements of the Bangladesh Operations.

### 33. Maturity Analysis

#### 33 (a) Bank

(i) An analysis of the total assets of the Bank as at December 31, based on the remaining period at the Balance Sheet date to the respective contractual maturity dates is given below:

	Up to 3 months Rs.'000	3 to 12 months Rs.'000	1 to 3 years Rs.'000	3 to 5 years Rs.'000	More than 5 years Rs.'000	Total as at 31.12.06 Rs.'000	Total as at 31.12.05 Rs.'000
<b>Interest Earning Assets</b>							
Cash and short-term funds	8,828,469	–	–	–	–	<b>8,828,469</b>	15,788,760
Balances with Central Banks	1,620,008	428,628	–	–	–	<b>2,048,636</b>	1,218,457
Government Treasury Bills and Bonds	11,675,920	364,389	–	–	–	<b>12,040,309</b>	11,410,083
Commercial paper	422,783	–	–	–	–	<b>422,783</b>	407,567
Securities purchased under resale agreements	4,593,089	–	–	–	–	<b>4,593,089</b>	808,135
Investments held to Maturity	98,500	669,387	434,999	50,452	–	<b>1,253,338</b>	1,814,103
Treasury Bonds maturing after one year	–	–	19,419,293	–	605,600	<b>20,024,893</b>	9,808,477
Loans and advances	67,778,837	25,168,220	32,721,331	12,244,898	12,618,753	<b>150,532,039</b>	118,763,027
	<u>95,017,606</u>	<u>26,630,624</u>	<u>52,575,623</u>	<u>12,295,350</u>	<u>13,224,353</u>	<b>199,743,556</b>	160,018,609
<b>Non-Interest Earning Assets</b>							
Cash and short-term funds	4,910,240	–	–	–	–	<b>4,910,240</b>	2,874,093
Balances with Central Banks	7,869,977	2,146,552	81,974	53,234	373,278	<b>10,525,015</b>	7,826,723
Dealing securities	144,896	–	–	–	–	<b>144,896</b>	182,243
Investments held for sale	131,842	86,550	–	–	–	<b>218,392</b>	–
Investments held to maturity	119,266	–	–	–	21,175	<b>140,441</b>	1,277,269
Investments in associate companies	–	–	–	–	44,331	<b>44,331</b>	107,081
Investments in subsidiary companies	–	–	–	–	433,681	<b>433,681</b>	433,681
Interest and fees receivable	1,638,893	–	–	–	–	<b>1,638,893</b>	1,183,626
Other assets	2,713,061	–	–	–	82,956	<b>2,796,017</b>	2,991,791
Property, Plant & Equipment	–	–	–	–	3,217,262	<b>3,217,262</b>	3,032,362
Intangible assets	–	–	–	–	161,529	<b>161,529</b>	149,985
	<u>17,528,175</u>	<u>2,233,102</u>	<u>81,974</u>	<u>53,234</u>	<u>4,334,212</u>	<b>24,230,697</b>	20,058,854
<b>Total Assets</b>	<b>112,545,781</b>	<b>28,863,726</b>	<b>52,657,597</b>	<b>12,348,584</b>	<b>17,558,565</b>	<b>223,974,253</b>	180,077,463
<b>Percentage - 31.12.06</b>	<b>50.25</b>	<b>12.89</b>	<b>23.51</b>	<b>5.51</b>	<b>7.84</b>	<b>100.00</b>	
Percentage - 31.12.05	54.96	15.48	15.86	5.45	8.25		100.00

(ii) An analysis of the total liabilities and shareholders' funds of the Bank as at December 31, based on the remaining period at the Balance Sheet date to the respective contractual maturity dates is given below:

	Up to 3 months Rs.'000	3 to 12 months Rs.'000	1 to 3 years Rs.'000	3 to 5 years Rs.'000	More than 5 years Rs.'000	Total as at 31.12.06 Rs.'000	Total as at 31.12.05 Rs.'000
<b>Interest Bearing Liabilities</b>							
Deposits from customers	103,620,353	28,329,639	931,771	612,107	5,259,444	<b>138,753,314</b>	115,224,576
Borrowings	6,068,836	9,905,262	2,272,465	235,190	462,363	<b>18,944,116</b>	13,425,857
Securities sold under repurchase agreements	12,169,829	2,152,758	7,419	–	–	<b>14,330,006</b>	11,389,174
Debentures	–	–	3,244,410	2,462,820	973,210	<b>6,680,440</b>	4,553,410
	<u>121,859,018</u>	<u>40,387,659</u>	<u>6,456,065</u>	<u>3,310,117</u>	<u>6,695,017</u>	<b>178,707,876</b>	144,593,017

	Up to 3 months Rs.'000	3 to 12 months Rs.'000	1 to 3 years Rs.'000	3 to 5 years Rs.'000	More than 5 years Rs.'000	Total as at 31.12.06 Rs.'000	Total as at 31.12.05 Rs.'000
<b>Non-Interest Bearing Liabilities</b>							
Deposits from customers	18,880,756	–	–	–	–	18,880,756	12,376,704
Dividends payable	112,500	–	–	–	–	112,500	230,352
Other liabilities	8,404,027	–	–	–	–	8,404,027	6,077,107
Tax payable	446,487	999,231	–	–	–	1,445,718	817,754
Deferred taxation	–	–	–	580,535	–	580,535	214,146
Share capital	–	–	1,000,000	–	1,428,186	2,428,186	3,327,364
Statutory Reserve Fund	–	–	–	–	1,428,500	1,428,500	1,421,000
Reserves	–	–	–	–	11,986,155	11,986,155	11,020,019
	27,843,770	999,231	1,000,000	580,535	14,842,841	45,266,377	35,484,446
<b>Total Liabilities</b>	<b>149,702,788</b>	<b>41,386,890</b>	<b>7,456,065</b>	<b>3,890,652</b>	<b>21,537,858</b>	<b>223,974,253</b>	<b>180,077,463</b>
<b>Percentage - 31.12.06</b>	<b>66.83</b>	<b>18.48</b>	<b>3.33</b>	<b>1.74</b>	<b>9.62</b>	<b>100.00</b>	
Percentage - 31.12.05	66.05	14.42	6.98	2.16	10.39		100.00

**33 (b) Group**

- (i) An analysis of the total assets of the Group as at December 31, based on the remaining period at the Balance Sheet date to the respective contractual maturity dates is given below:

	Up to 3 months Rs.'000	3 to 12 months Rs.'000	1 to 3 years Rs.'000	3 to 5 years Rs.'000	More than 5 years Rs.'000	Total as at 31.12.06 Rs.'000	Total as at 31.12.05 Rs.'000
<b>Interest Earning Assets</b>							
Cash and short-term funds	8,828,469	–	–	–	–	8,828,469	15,788,760
Balances with Central Banks	1,620,008	428,628	–	–	–	2,048,636	1,218,457
Government Treasury Bills and Bonds	11,857,382	364,389	–	–	–	12,221,771	11,665,496
Commercial paper	422,783	–	–	–	–	422,783	407,567
Securities purchased under resale agreements	4,593,089	–	–	–	–	4,593,089	808,135
Investments held to maturity	98,500	669,387	434,999	50,452	–	1,253,338	1,814,103
Treasury Bonds maturing after one year	–	–	19,419,293	–	605,600	20,024,893	9,808,477
Loans and advances	67,778,209	25,138,377	32,650,954	12,243,557	12,618,752	150,429,849	118,679,369
	95,198,440	26,600,781	52,505,246	12,294,009	13,224,352	199,822,828	160,190,364
<b>Non-Interest Earning Assets</b>							
Cash and short-term funds	4,902,970	–	–	–	–	4,902,970	2,867,999
Balances with Central Banks	7,869,977	2,146,552	81,974	53,234	373,278	10,525,015	7,826,723
Dealing securities	144,896	–	–	–	–	144,896	182,243
Investments held for sale	140,555	260,704	–	–	–	401,259	–
Investments held to maturity	119,266	–	–	–	21,275	140,541	1,277,369
Investments in associate companies	–	–	–	–	40,965	40,965	282,789
Interest and fees receivable	1,638,893	–	–	–	–	1,638,893	1,198,631
Other assets	2,722,494	–	–	–	120,488	2,842,982	2,919,779
Property, Plant & Equipment	–	–	–	–	3,437,522	3,437,522	3,238,039
Intangible assets	–	–	–	1,239	161,529	162,768	151,115
	17,539,051	2,407,256	81,974	54,473	4,155,057	24,237,811	19,944,687
<b>Total Assets</b>	<b>112,737,491</b>	<b>29,008,037</b>	<b>52,587,220</b>	<b>12,348,482</b>	<b>17,379,409</b>	<b>224,060,639</b>	<b>180,135,051</b>
<b>Percentage - 31.12.06</b>	<b>50.31</b>	<b>12.95</b>	<b>23.47</b>	<b>5.51</b>	<b>7.76</b>	<b>100.00</b>	
Percentage - 31.12.05	55.03	15.46	15.82	5.45	8.24		100.00

## Notes to the Financial Statements

(ii) An analysis of the total liabilities and shareholders' funds of the Group as at December 31, based on the remaining period at the Balance Sheet date to the respective contractual maturity dates is given below:

	Up to 3 months Rs.'000	3 to 12 months Rs.'000	1 to 3 years Rs.'000	3 to 5 years Rs.'000	More than 5 years Rs.'000	Total as at 31.12.06 Rs.'000	Total as at 31.12.05 Rs.'000
<b>Interest Bearing Liabilities</b>							
Deposits from customers	103,620,008	28,329,639	931,771	612,107	5,259,444	<b>138,752,969</b>	115,114,009
Borrowings	6,068,836	9,905,262	2,272,465	235,190	462,363	<b>18,944,116</b>	13,425,857
Securities sold under repurchase agreements	12,156,886	2,152,758	7,419	-	-	<b>14,317,063</b>	11,386,147
Debentures	-	-	3,244,410	2,462,820	973,210	<b>6,680,440</b>	4,553,410
	<u>121,845,730</u>	<u>40,387,659</u>	<u>6,456,065</u>	<u>3,310,117</u>	<u>6,695,017</u>	<b><u>178,694,588</u></b>	<u>144,479,423</u>
<b>Non-Interest Bearing Liabilities</b>							
Deposits from customers	18,778,859	-	-	-	-	<b>18,778,859</b>	12,376,704
Dividends payable	112,500	-	-	-	-	<b>112,500</b>	230,352
Other liabilities	8,402,043	-	-	-	-	<b>8,402,043</b>	6,070,129
Tax payable	414,961	1,005,265	-	-	-	<b>1,420,226</b>	784,218
Deferred taxation	-	-	580,534	44,406	-	<b>624,940</b>	227,367
Share capital	-	-	1,000,000	-	1,428,186	<b>2,428,186</b>	3,327,364
Statutory Reserve Fund	-	-	-	-	1,429,319	<b>1,429,319</b>	1,421,819
Reserves	-	-	-	-	12,158,955	<b>12,158,955</b>	11,204,390
Minority Interest	-	-	-	-	11,023	<b>11,023</b>	13,285
	<u>27,708,363</u>	<u>1,005,265</u>	<u>1,580,534</u>	<u>44,406</u>	<u>15,027,483</u>	<b><u>45,366,051</u></b>	<u>35,655,628</u>
<b>Total Liabilities</b>	<b><u>149,554,093</u></b>	<b><u>41,392,924</u></b>	<b><u>8,036,599</u></b>	<b><u>3,354,523</u></b>	<b><u>21,722,500</u></b>	<b><u>224,060,639</u></b>	<b><u>180,135,051</u></b>
<b>Percentage - 31.12.06</b>	<b><u>66.75</u></b>	<b><u>18.47</u></b>	<b><u>3.59</u></b>	<b><u>1.50</u></b>	<b><u>9.69</u></b>	<b><u>100.00</u></b>	
Percentage - 31.12.05	65.87	14.48	6.98	2.17	10.50		100.00

Notes (i) Loans and advances are shown net of interest in suspense and provision for bad & doubtful debts.

(ii) Balances with Central Banks have been apportioned into the maturity groups based on the maturity pattern of the deposits liable for Statutory Reserve Requirements.

(iii) Demand and savings deposits have been classified into the up to 3 months category. However, the major part of these deposits represents core retail deposits with longer term maturity.

(iv) Shareholders' funds excluding Cumulative Redeemable Preference Shares are classified into the more than 5 years category since no contractual date of maturity can be identified. However, these funds are available and have in fact been used for financing assets with lesser maturity periods.

### 34. Commitments and Contingencies

34 (a) In the normal course of business the Bank makes various irrevocable commitments and incurs certain contingent liabilities with legal recourse to its customers. Even though these obligations may not be recognised on the balance sheet, they do contain credit risk and are therefore form part of the overall risk of the Bank. No material losses are anticipated as a result of these transactions.

	Bank		Group	
	2006 Rs.'000	2005 Rs.'000	2006 Rs.'000	2005 Rs.'000
<b>Commitments</b>				
Commitments for unutilised facilities (direct advances)	<b>14,293,339</b>	14,248,496	<b>14,293,339</b>	14,248,496
<b>Contingent Liabilities</b>				
Acceptances	<b>4,937,977</b>	4,517,958	<b>4,937,977</b>	4,517,958
Documentary credits	<b>9,591,240</b>	9,373,307	<b>9,591,240</b>	9,373,307
Guarantees	<b>17,432,290</b>	14,064,651	<b>17,432,290</b>	14,064,651
Bills for collection	<b>5,016,267</b>	4,346,833	<b>5,016,267</b>	4,346,833
	<u><b>36,977,774</b></u>	<u>32,302,749</u>	<u><b>36,977,774</b></u>	<u>32,302,749</u>
Forward exchange contracts (net)	<b>2,352,805</b>	602,708	<b>2,352,805</b>	602,708
	<u><b>39,330,579</b></u>	<u>32,905,457</u>	<u><b>39,330,579</b></u>	<u>32,905,457</u>
Total commitments and contingencies	<b><u>53,623,918</u></b>	<u>47,153,953</u>	<b><u>53,623,918</u></b>	<u>47,153,953</u>

**34 (b) Litigation against the Bank**

Litigation is a common occurrence in the banking industry due to the nature of the business. The Bank has an established protocol for dealing with such legal claims. Once professional advice has been obtained and the amount of damages reasonably estimated, the Bank makes adjustments to account for any adverse effects which the claims may have on its financial standing. At year end, the Bank had several such unresolved legal claims.

- (i) Court action has been initiated by a customer in proceedings Number 36/96 (i) to claim a sum of Rs. 183.050 million on account of a forward exchange contract. Judgement was delivered in favour of the Bank dismissing the plaintiff's action but the plaintiff has appealed against the judgement. The Bank is defending the action.
- (ii) Judgement was delivered on September 21, 1995 on the Court action initiated by a customer in proceedings Number 93650/M to claim a sum of approximately Rs. 6.000 million relating to a dispute over the payment by the Bank of several cheques alleged to have been forged. The Bank has appealed against the judgement. The judgement relating to the appeal has been reserved.
- (iii) Three Labour Tribunal cases filed by three ex-employees on termination of employment are pending against the Bank. In addition, the Bank has appealed against the order of the Labour Tribunal in three other cases.
- (iv) Court action has been initiated by a customer in proceedings Number 25831/MR to claim a sum of Rs. 2.880 million together with interest o/a of an interest refund claimed on a Current Account. Written submissions have been filed by both parties. Judgement due on March 29, 2007.
- (v) Court action has been initiated by a customer in proceedings Number 282/2002 (1) restraining the Bank from paying a sum of Rs. 13.350 million on a bank guarantee. The case has been referred to Commercial High Court and is yet to be called up. The Bank has obtained a counter guarantee from an insurance company.
- (vi) Court action has been initiated by a customer in proceedings Number 27485/MR to recover a sum of Rs. 15.204 million in damages in relation to alleged wrongful payment of a cheque for Rs. 0.024 million and alleged incorrect remark on two other cheques for values of Rs. 0.500 million and Rs. 0.180 million that have been returned. Bank is defending the action.
- (vii) Court action has been initiated by a customer in proceedings Number 25085/MR to recover a sum of US \$ 27,500 alleged to have been paid by the Bank by debiting the account without authority of the customer. Bank has paid this amount in pursuance of a counter guarantee issued by the Bank. Both parties are required to file written submissions on March 30, 2007.
- (viii) Court action has been initiated by a customer in proceedings Number 36542/MR to recover a sum of Rs. 0.400 million and interest thereon and a further sum of Rs. 1.000 million from the Bank on an alleged breach of contract. Legal opinion has been obtained by the Bank and the Bank is defending the action.
- (ix) Court action has been initiated by a customer in proceedings Number 1336/M to claim a sum of Rs. 0.200 million and interest thereon relating to a dispute over the alleged non-payment by the Bank of two cheques when instructions were given to honour them and alleged payment by the Bank of another cheque when instructions were given not to do so. The Bank is defending the action.
- (x) Court action has been initiated by a person against the Bank and an executive of the Bank in proceedings Number 45937/MR to claim a sum of Rs. 20.000 million for allegedly advising a customer of the Bank against signing as a guarantor for a loan to be obtained by the person from a finance company. The Bank is defending the action.

## Notes to the Financial Statements

### 35. Capital Commitments

Capital expenditure approved by the Board of Directors for which provision has not been made in these Financial Statements amounted to approximately:

	Bank		Group	
	2006 Rs.'000	2005 Rs.'000	2006 Rs.'000	2005 Rs.'000
Approved and contracted for	186,920	5,711	186,920	5,711
Approved but not contracted for	45,350	24,950	45,350	24,950
	<b>232,270</b>	<b>30,661</b>	<b>232,270</b>	<b>30,661</b>

### 36. Financial Reporting by Segment as per the Provisions of Sri Lanka Accounting Standard No. 28 - Group

#### (a) Business Segments

For the year ended December 31,	Banking		Leasing		Dealing		Property/ Investments		Eliminations/ Unallocated		Total	
	2006 Rs.'000	2005 Rs.'000	2006 Rs.'000	2005 Rs.'000	2006 Rs.'000	2005 Rs.'000	2006 Rs.'000	2005 Rs.'000	2006 Rs.'000	2005 Rs.'000	2006 Rs.'000	2005 Rs.'000
<b>Revenue from external customers</b>												
Interest	15,799,299	10,203,897	-	-	2,612,078	2,258,180	-	-	-	-	18,411,377	12,462,077
Exchange profit	785,387	97,047	-	-	653,621	489,868	-	-	-	-	1,439,008	586,915
Lease income	-	-	1,125,851	831,741	-	-	-	-	-	-	1,125,851	831,741
Commissions	2,010,197	1,756,609	-	-	994	3,010	-	-	-	-	2,011,191	1,759,619
Other income	278,790	205,078	-	-	4,730	(64,585)	1,014,302	338,836	166,617	105,696	1,464,439	585,025
Total revenue from external customers	18,873,673	12,262,631	1,125,851	831,741	3,271,423	2,686,473	1,014,302	338,836	166,617	105,696	24,451,866	16,225,377
Inter-segment revenue	-	-	-	-	-	-	-	-	-	-	-	-
Total revenue	18,873,673	12,262,631	1,125,851	831,741	3,271,423	2,686,473	1,014,302	338,836	166,617	105,696	24,451,866	16,225,377
Segment result	5,545,303	3,515,591	659,677	802,716	354,638	314,781	1,014,302	338,836	166,617	105,696	7,740,537	5,077,620
<b>Unallocated expenses</b>											(3,481,838)	(1,510,034)
Profit from operations											4,258,699	3,567,586
Net financing costs											-	-
Income from associates											62,454	100,462
Income tax expense											(2,248,751)	(1,309,969)
Minority interest											(1,695)	(1,641)
Net profit for the year											2,070,707	2,356,438

As at December 31,	Banking		Leasing		Dealing		Property/ Investments		Eliminations/ Unallocated		Total	
	2006 Rs.'000	2005 Rs.'000	2006 Rs.'000	2005 Rs.'000	2006 Rs.'000	2005 Rs.'000	2006 Rs.'000	2005 Rs.'000	2006 Rs.'000	2005 Rs.'000	2006 Rs.'000	2005 Rs.'000
<b>Other Information</b>												
Segment assets	165,603,473	122,523,252	9,421,479	7,005,167	39,536,550	39,693,679	1,538,775	3,273,715	7,919,397	7,356,449	224,019,674	179,852,262
Investment in associates	-	-	-	-	-	-	40,965	282,789	-	-	40,965	282,789
Unallocated assets	-	-	-	-	-	-	-	-	-	-	-	-
Total assets											224,060,639	180,135,051
Segment liabilities	147,048,178	106,792,334	9,421,479	7,005,167	39,536,550	39,693,679	1,579,740	3,556,504	10,447,209	7,120,509	208,033,156	164,168,193
Unallocated liabilities	-	-	-	-	-	-	-	-	-	-	-	-
Total liabilities											208,033,156	164,168,193
<b>For the year</b>												
December 31,	2006 Rs.'000	2005 Rs.'000	2006 Rs.'000	2005 Rs.'000	2006 Rs.'000	2005 Rs.'000	2006 Rs.'000	2005 Rs.'000	2006 Rs.'000	2005 Rs.'000	2006 Rs.'000	2005 Rs.'000

**Information on Cash Flows**

Cash flows from												
operating activities	(1,694,424)	2,402,736	(1,756,635)	(1,524,422)	354,638	314,781	-	-	(19,460)	(28,349)	(3,115,881)	1,164,746
Cash flows from												
investing activities	1,961,187	122,404	-	-	(11,637,215)	643,163	821,145	(489,385)	-	-	(8,854,883)	276,182
Cash flows from												
financing activities	4,769,519	5,224,080	-	-	1,737,103	-	-	-	1,163,934	586,599	7,670,556	5,810,679
Capital expenditure	(594,713)	(572,493)	-	-	-	-	(30,399)	(158,071)	-	-	(625,112)	(730,564)

**(b) Geographical Segments**

	Bank				Group			
	2006		2005		2006		2005	
	Rs.'000	%	Rs.'000	%	Rs.'000	%	Rs.'000	%
<b>Assets</b>								
Domestic Operations	184,674,125	82.45	144,922,969	80.48	184,760,511	82.46	144,980,557	80.49
Overseas Operations	16,555,284	7.39	13,104,682	7.28	16,555,284	7.39	13,104,682	7.27
Off-shore Banking Centre	22,744,844	10.16	22,049,812	12.24	22,744,844	10.15	22,049,812	12.24
	<u>223,974,253</u>	<u>100.00</u>	<u>180,077,463</u>	<u>100.00</u>	<u>224,060,639</u>	<u>100.00</u>	<u>180,135,051</u>	<u>100.00</u>
<b>Income</b>								
Domestic Operations	20,799,141	85.00	13,293,660	82.58	20,781,537	84.99	13,419,392	82.70
Overseas Operations	1,884,133	7.70	1,591,320	9.88	1,884,133	7.71	1,591,320	9.81
Off-shore Banking Centre	1,786,196	7.30	1,214,665	7.54	1,786,196	7.30	1,214,665	7.49
	<u>24,469,470</u>	<u>100.00</u>	<u>16,099,645</u>	<u>100.00</u>	<u>24,451,866</u>	<u>100.00</u>	<u>16,225,377</u>	<u>100.00</u>
<b>Profit before Tax</b>								
Domestic Operations	2,818,739	66.90	2,684,558	73.71	2,926,347	67.73	2,710,646	73.90
Overseas Operations	809,971	19.22	451,639	12.40	809,971	18.74	451,639	12.31
Off-shore Banking Centre	584,835	13.88	505,763	13.89	584,835	13.53	505,763	13.79
	<u>4,213,545</u>	<u>100.00</u>	<u>3,641,960</u>	<u>100.00</u>	<u>4,321,153</u>	<u>100.00</u>	<u>3,668,048</u>	<u>100.00</u>
<b>Profit after Tax</b>								
Domestic Operations	1,148,360	57.06	1,842,787	77.94	1,208,134	58.29	1,836,626	77.89
Overseas Operations	385,387	19.15	121,775	5.15	385,387	18.60	121,775	5.16
Off-shore Banking Centre	478,881	23.79	399,678	16.91	478,881	23.11	399,678	16.95
	<u>2,012,628</u>	<u>100.00</u>	<u>2,364,240</u>	<u>100.00</u>	<u>2,072,402</u>	<u>100.00</u>	<u>2,358,079</u>	<u>100.00</u>

**37. Directors' Interests in Contracts with the Company**

Company	Relationship	Accommodation Granted/Deposit	Balance Outstanding As at 31.12.06 Rs.	Balance Outstanding As at 31.12.05 Rs.
<b>(a) Mr. M.J.C. Amarasuriya</b>				
Pelwatte Sugar Ind. (Pvt.) Ltd.	Chairman	Loans & Advances	22,933,430	16,406,859
		Off Balance Sheet Accommodations	1,170,563	–
		Deposits	42,013,796	39,574,946
Serendib Flour Mills (Pvt.) Ltd.	Chairman	Loans & Advances	339,439,803	202,214,341
		Off Balance Sheet Accommodations	61,072,739	324,993,888
		Deposits	86,068,046	60,466,147
Unimo Enterprises Ltd.	Chairman	Loans & Advances	112,691,380	98,823,339
		Off Balance Sheet Accommodations	32,074,322	3,511,534
		Deposits	18,445	–
United Motors Lanka Ltd.	Chairman (since resigned)	Loans & Advances	97,239,058	273,625,286
		Off Balance Sheet Accommodations	39,850,159	14,896,919
		Deposits	178,394	11,173,130
Property Development Ltd.	Chairman	Deposits	3,005,527	157,836
UML Agencies & Distributors Ltd.	Chairman	Deposits	118	–
Unawatuna Beach Resorts Ltd.	Chairman	Deposits	95	36,227
Orient Motor Company Ltd.	Director	Loans & Advances	60,487,723	93,163,086
		Off Balance Sheet Accommodations	–	–
		Deposits	–	–
TVS Lanka (Pvt) Ltd.	Director	Deposits	32,056	5,682

Mr. M.J.C. Amarasuriya, the Chairman of the Bank is also the Chairman of ONEzero Company Ltd., X-pertise Ltd., Commercial Fund Management (Pvt) Ltd., Commercial Bank Primary Dealer Ltd. and Equity Investments Lanka Ltd., Director of Commercial Leasing Company Ltd. and Technoconsult (Pvt) Ltd. He is also a Co-owner of Clodagh Western Estate. He is a Council Member of the University of Colombo - Science Faculty.

Company	Relationship	Accommodation Granted/Deposit	Balance Outstanding As at 31.12.06 Rs.	Balance Outstanding As at 31.12.05 Rs.
<b>(b) Mr. J.S. Mather (Resigned on March 16, 2006)</b>				
Acme Printing & Packaging	Director	Loans & Advances	15,718,340	13,804,669
		Off Balance Sheet Accommodations	–	4,543,440
		Deposits	144,838	126,203
Chemical Industries (Colombo) Ltd.	Director	Loans & Advances	227,314	62,547,210
		Off Balance Sheet Accommodations	49,922,438	10,015,558
		Deposits	403,664	24,909,795
David Peiris Motor Co. Ltd.	Director	Deposits	44,491,838	6,985,493
Delmage Forsyth & Co. Ltd.	Director	Deposits	53,627	52,508

Mr. J.S. Mather, former Deputy Chairman (resigned on March 16, 2006) of the Bank was also a Director of Commercial Bank Primary Dealer Ltd., Commercial Development Co. Ltd. and Onezero Co. Ltd. He is a Director of Castallys (Pvt) Ltd., Comark Lanka (Pvt) Ltd., Delair Ltd., Delmege Air Services (Pvt) Ltd., Delmege Forsyth & Co (Shipping) Ltd., Lanka Aluminium Industries Ltd., Lanka Tours & Trades (Pvt) Ltd., Management Systems Ltd., Managers & Secretaries (Pvt) Ltd., Navigator Management (Pvt) Ltd. and SS L Business Services (Pvt) Ltd., a Partner of Lanka Tours & Trades Properties.

Company	Relationship	Accommodation Granted/Deposit	Balance Outstanding As at 31.12.06 Rs.	Balance Outstanding As at 31.12.05 Rs.
<b>(c) Mr. B.R.L. Fernando</b>				
Chemanex Ltd.	Chairman	Loans & Advances	12,126,609	20,705,894
		Off Balance Sheet Accommodations	13,832,994	24,635,607
		Deposits	87,323	21,153,573
Chemical Industries (Colombo) Ltd.	Chairman	Loans & Advances	227,314	62,547,210
		Off Balance Sheet Accommodations	49,922,438	10,015,558
		Deposits	403,664	24,909,795
CIC Agri Bio Tech (Pvt.) Ltd.	Chairman	Loans & Advances	-	1,836,683
		Off Balance Sheet Accommodations	-	5,958,000
		Deposits	5,425,474	-
CIC Feeds (Pvt.) Ltd.	Chairman	Loans & Advances	473,596,099	463,211,135
		Off Balance Sheet Accommodations	82,349,259	396,398,063
		Deposits	750,594	-
CIC Fertilizers (Pvt.) Ltd.	Chairman	Loans & Advances	304,233,993	641,450,000
		Off Balance Sheet Accommodations	4,028,866	77,737,543
		Deposits	377,779	-
CIC Seeds (Pvt.) Ltd.	Chairman	Loans & Advances	56,795	8,654,456
		Off Balance Sheet Accommodations	7,579,119	41,383,802
		Deposits	981,916	807,889
CIC Vet Care (Pvt.) Ltd.	Chairman	Loans & Advances	61,970,189	51,317,047
		Off Balance Sheet Accommodations	19,437,128	39,110,799
		Deposits	2,000,070	2,200,845
Cisco Speciality Packaging (Pvt.) Ltd.	Chairman	Loans & Advances	41,230,509	16,900,000
		Off Balance Sheet Accommodations	-	19,187,811
		Deposits	-	5,807,261
CIC Paints (Pvt.) Ltd.	Chairman	Deposits	9,452,236	4,835,687
CIC Environmental Management Liquid (Pvt) Ltd.	Chairman	Deposits	2,636	2,886
CIC Poultry Farms Ltd.	Chairman	Deposits	2,125,155	-
Paints & General Industries Ltd.	Director	Loans & Advances	199,463,924	349,630,984
		Off Balance Sheet Accommodations	13,578,847	11,394,467
		Deposits	349,237,194	171,638
Rainwear (Pvt) Ltd.	Director	Loans & Advances (US\$)	186,544	138,112
		Off Balance Sheet Accommodations	-	-
		Deposits	318,393	142,957
The Lighthouse Hotel Ltd.	Director	Loans & Advances	8,077,812	-
		Off Balance Sheet Accommodations	-	-
		Deposits	379,548	371,691
Agro Enterprises Japan-Lanka (Pvt) Ltd.	Director	Deposits	434,935	-
Premier Electronics (Pvt) Ltd.	Director	Deposits	106,414	257,286
Link Natural Products (Pvt) Ltd.	Director	Deposits	330,810	2,156,355
Employees' Trust Fund	Director	Deposits	12,914,034	8,293,409

Mr. B.R.L Fernando, the Deputy Chairman of the Bank is also the Chairman of CIC Bio Security Breeder Farms Ltd., Mercantile Service Provident Society and Co-Chairman of Catholic Business Persons & Professionals. He is a Director of Commercial Bank Primary Dealer Ltd., Crop Management Services (Pvt) Ltd., National Enterprise Development Authority, First Capital Equities (Pvt) Ltd. and T-Plus (Pvt) Ltd. He is also the Trustee to Employers' Federation of Ceylon Ltd. and immediate past President of Japan-Sri Lanka Technical & Cultural Association.

## Notes to the Financial Statements

Company	Relationship	Accommodation Granted/Deposit	Balance Outstanding As at 31.12.06 Rs.	Balance Outstanding As at 31.12.05 Rs.
<b>(d) Mr. A.L. Gooneratne</b>				
Commercial Insurance Brokers (Pvt.) Ltd.	Director	Loans & Advances	48,401,000	84,394,281
		Off Balance Sheet Accommodations	2,625,000	2,650,000
		Deposits	14,766,362	4,642,613

Mr. A.L. Gooneratne, the Managing Director of the Bank is also a Director of Commercial Leasing Co. Ltd., Commercial Development Co. Ltd., Commercial Fund Management (Pvt) Ltd., Equity Investments Lanka Ltd., Commercial Bank Primary Dealer Ltd., ONEzero Co. Ltd. and X-pertise Ltd.

**(e) Dr. H.S. Wanasinghe**

A Director of the Bank is also a Director of Commercial Development Co. Ltd.

Company	Relationship	Accommodation Granted/Deposit	Balance Outstanding As at 31.12.06 Rs.	Balance Outstanding As at 31.12.05 Rs.
<b>(f) Mr. A.N. Fonseka</b>				
Post Graduate Institute of Management University of Sri Jayawardenepura	Member Governing Board	Loans & Advances	310,730	778,408
		Off Balance Sheet Accommodations	-	-
		Deposits	-	-
Colombo Stock Exchange	Chairman	Deposits	1,127,739	457,944
DFCC Stock Brokers (Pvt) Ltd.	Chairman	Deposits	168,692	2,255,380
Lanka Industrial Estates Ltd.	Chairman	Deposits	29,712,891	24,656,186
Lanka Ventures Ltd.	Chairman	Deposits	132,448	132,698
National Asset Management Ltd.	Director	Deposits	392,643	76,591

Mr. A.N. Fonseka, a Director of the Bank is the General Manager/Chief Executive of DFCC Bank. He is also the Chairman of DFCC Consulting (Pvt) Ltd. and Synapsys Ltd. He is a Director of Onezero Company Ltd., Commercial Bank Primary Dealer Ltd. and Credit Information Bureau of Sri Lanka. He is a Member of the Governing Board of National Institute of Business Management.

Company	Relationship	Accommodation Granted/Deposit	Balance Outstanding As at 31.12.06 Rs.	Balance Outstanding As at 31.12.05 Rs.
<b>(g) Mr. L.J.A. Fernando</b>				
Standard Trading Company Ltd.	Managing Director	Loans & Advances	1,462,256	1,426,256
		Off Balance Sheet Accommodations	-	-
		Deposits	-	-

Mr. L.J.A. Fernando, a Director of the Bank is also a Director at Classic International (Pvt) Ltd., L.F. Holdings (Pvt) Ltd., L.F. Teas (Pvt) Ltd., STC Logistics (Pvt) Ltd., STC Trading House (Pvt) Ltd., Motor Marvels (Pvt) Ltd., Frontier Automotive (Pvt) Ltd., Koboshu Corporation (Pvt) Ltd., Horana Plantations Ltd., Unidil Packaging (Pvt) Ltd., Ceytea Plantation Management Ltd., Research International (Pvt) Ltd. and Marlinkspike Property Developers (Pvt) Ltd.

Company	Relationship	Accommodation Granted/Deposit	Balance Outstanding As at 31.12.06 Rs.	Balance Outstanding As at 31.12.05 Rs.
<b>(h) Mr. D.S. Weerakkody</b>				
Cornucopia Lanka Ltd.	Managing Director	Deposits	8,700	9,350
Chartered Institute of Management Accountants	Council Member	Deposits	20,523,735	2,430,548

Mr. D.S. Weerakkody, a Director of the Bank is also a Director of the DFCC Bank and SmithKline Beecham Ltd. He is also a Council Member of Sri Lanka Tennis Association.

**(i) Mr. Iyad M. Malas**

A Director of the Bank is the Director of IFC South Asia.

Company	Relationship	Accommodation Granted/Deposit	Balance Outstanding As at 31.12.06 Rs.	Balance Outstanding As at 31.12.05 Rs.
<b>(j) Deshamanya Ken Balendra</b>				
Brandix Lanka Ltd.	Chairman	Loans & Advances (US\$)	3,200,000	4,500,000
		Off Balance Sheet Accommodations (US\$)	–	–
		Deposits (US\$)	2,230	1,723
Ceylon Tobacco Co. Ltd.	Chairman	Loans & Advances	24,808,871	–
		Off Balance Sheet Accommodations	–	–
		Deposits	1,001,474,207	6,688,972
Brandix Finishing Ltd.	Director	Loans & Advances (US\$)	1,025,981	293,472
		Off Balance Sheet Accommodations (US\$)	–	–
		Deposits (US\$)	11,237	–
Brandix Apparel Ltd.	Director	Loans & Advances (US\$)	644,732	–
		Off Balance Sheet Accommodations (US\$)	–	–
		Deposits (US\$)	800,064	550,788
Brandix Casual Wear Ltd.	Director	Loans & Advances (US\$)	324,704	748,189
		Off Balance Sheet Accommodations (US\$)	63,223	772,986
		Deposits (US\$)	–	–
Brandix Intimate Apparels Ltd.	Director	Loans & Advances (US\$)	292,915	115,108
		Off Balance Sheet Accommodations (US\$)	–	–
		Deposits	1,031,935	2,480,191
Phoenix Ventures Ltd.	Director	Loans & Advances	–	–
		Off Balance Sheet Accommodations	–	–
		Deposits	468,472	148,246
Caltex Lubricants Lanka Ltd.	Director	Deposits	270,659	99,500

Deshamanya Ken Balendra, a Director of the Bank is also the Chairman of South Asia Regional Fund sponsored by the Commonwealth Development Corporation, Aureos Lanka Advisers Ltd - Investment Committee. He is a Director of Galle Face Hotels Ltd.

(k) The following credit card facilities were outstanding as at December 31. The provision of Section 47 of the Banking Act No. 30 of 1988 have been complied with.

Name of Director	Position	As at 31.12.06		As at 31.12.05	
		Balance Outstanding Rs.	Security Value Rs.	Balance Outstanding Rs.	Security Value Rs.
Mr. A.L. Gooneratne	Managing Director	21,241	300,000	–	–
Dr. H.S. Wanasinghe	Director	48,052	339,062	38,772	316,289

### 38. Related Party Transactions

#### 38.1 Transactions with Key Managerial Persons

**38.1.1** Key Managerial Persons include members of the Board of Directors of the Bank and Key Employees of the Bank holding directorships in Subsidiary and Associate Companies of the Bank.

The Bank carries out transactions in the ordinary course of its business on an arm's length basis at commercial rates with Key Managerial Persons. The Weighted Average Prime Lending Rate published by the Central Bank of Sri Lanka for the weeks ended June 30, 2006 and December 31, 2006 were 12.63% p.a. and 15.19% p.a. respectively. Except the loans that the Key Managerial persons have availed under the loan schemes uniformly applicable to all the staff at concessionary rates, the facilities granted to the Key Managerial Persons listed below have been at or above the prime lending rate that prevailed at the time of granting the facilities.

**38.1.2** Loans & Advances in the names of Key Managerial Persons and their close family members are given below:

<i>As at December 31,</i>	<b>2006</b>	2005
	<b>Rs.</b>	Rs.
Loans & Advances and other credit facilities	<b>66,245,651</b>	63,338,856

**38.1.3** Directors' remuneration amounted to Rs. 33.074 million for the year 2006 (Rs. 27.851 million for 2005).

**38.1.4** Post employment benefits paid to past Directors of the Bank amounted to Rs. 1.897 million for the year 2006 (Rs. 1.881 million for 2005).

**38.1.5** The cumulative options allotted to Key Managerial Persons of the Bank under the Employee Share Option Plan (ESOP) 2002 were as follows:

<i>As at December 31,</i>	<b>2006</b>	2005
No. of cumulative options allotted	<b>785,970</b>	534,226

Note:

Non-Executive Directors of the Board are not entitled for options under the ESOP 2002.

**38.1.6** Credit Card outstanding balances of Key Managerial Persons were as follows:

<i>As at December 31,</i>	<b>2006</b>	2005
	<b>Rs.</b>	Rs.
Credit card outstanding balances	<b>339,151</b>	274,856

**38.2 Entities controlled by Key Managerial Persons**

The outstanding balances of Loans & Advances and other credit facilities of the entities in which the Key Managerial Persons have controlling interests, are given below:

<i>As at December 31,</i>	<b>2006</b>	2005
	<b>Rs.</b>	Rs.
<b>Clodagh Western Estate</b>		
Loans & Advances	<b>335,683</b>	306,219
Off Balance Sheet Accommodations	-	-

**38.3 Transactions with Subsidiary Companies**

The outstanding balances of Loans & Advances, other credit facilities and Deposits of the Subsidiary Companies of the Bank are given below:

<i>As at December 31,</i>	<b>2006</b>	2005
	<b>Rs.</b>	Rs.
<b>Commercial Development Co.Ltd.</b>		
Loans & Advances	<b>114,162,657</b>	84,749,474
Off Balance Sheet Accommodations	-	-
Deposits	<b>99,842,162</b>	94,109,465
<b>ONEzero Co. Ltd.</b>		
Loans & Advances	-	-
Off Balance Sheet Accommodations	<b>1,918,147</b>	-
Deposits	<b>2,048,921</b>	16,103,079
<b>Commercial Bank Primary Dealer Ltd.</b>		
Loans & Advances	-	-
Off Balance Sheet Accommodations	-	-
Deposits	<b>8,707,285</b>	8,901,560
<b>X-Pertise Ltd.</b>		
Loans & Advances	<b>396,373</b>	355,254
Off Balance Sheet Accommodations	-	-
Deposits	<b>345,409</b>	353,929
<b>Total</b>		
Loans & Advances	<b>114,559,030</b>	85,104,728
Off Balance Sheet Accommodations	<b>1,918,147</b>	-
Deposits	<b>110,943,777</b>	119,468,033

### 38.4 Transactions with Associate Companies

The outstanding balances of Loans & Advances, other credit facilities and Deposits of the Associate Companies of the Bank are as follows:

<i>As at December 31,</i>	<b>2006</b>	2005
	<b>Rs.</b>	Rs.
<b>Commercial Leasing Co. Ltd.</b>		
Loans & Advances	<b>921,465,899</b>	942,222,863
Off Balance Sheet Accommodations	<b>13,914,443</b>	5,668,458
Deposits	<b>31,737,466</b>	47,685,014
<b>Equity Investments Lanka Ltd.</b>		
Loans & Advances	<b>1,194,161</b>	-
Off Balance Sheet Accommodations	-	-
Deposits	<b>1,686,213</b>	1,988,626
<b>Total</b>		
Loans & Advances	<b>922,660,060</b>	942,222,863
Off Balance Sheet Accommodations	<b>13,914,443</b>	5,668,458
Deposits	<b>33,423,679</b>	49,673,640

### 38.5 Other Related Parties

The outstanding balances of Loans & Advances, other credit facilities and Deposits of other related parties of the Bank are as follows:

<i>As at December 31,</i>	<b>2006</b>	2005
	<b>Rs.</b>	Rs.
<b>DFCC Bank</b>		
Loans & Advances	-	-
Off Balance Sheet Accommodations	-	-
Deposits	<b>36,240,899</b>	31,129,612

### 38.6 Retirement Pension Fund and Widows' and Orphans' Pension (W&OP) Scheme

During the year, the Board of Directors having considered various adverse implications of the current pension scheme of the Bank, approved a restructured plan, designed by Hewitt Outsourcing Services (India) Ltd., aimed at converting the current pension scheme from a Defined Benefit Plan to a Defined Contribution Plan.

The Bank provided Rs. 1,811.594 million and Rs. 2.241 million to Pension Fund & W&OP Scheme respectively for the year ended December 31, 2006. (Rs. 229.454 million and Rs. 6.517 million for the Pension Fund & W&OP Scheme respectively for the year ended December 31, 2005).

**39. Interest Rate Swaps**

- (a) The Bank has entered into a swap agreement with Commercial Leasing Company, which is an Associate Company of the Bank, for a notional value of Rs. 500.000 million for a period of 3 years in August 2005, where the Bank pays interest at a floating rate at the Average Weighted Prime Lending Rate (AWPLR), whereas Commercial Leasing Company pays interest at a fixed rate of 12.50% p.a. Further, the Bank received Rs. 2.500 million as a commitment fee for facilitating the swap arrangement.
- (b) The Bank has entered into a swap agreement with the Hongkong and Shanghai Banking Corporation Ltd. (HSBC) for a notional value of US \$ 5.000 million for a period of 3 years in September 2006, where the Bank pays interest at a floating rate at 6 months London Inter-Bank Offered Rate (LIBOR), whereas HSBC Ltd. pays interest at a fixed rate of 5.12% p.a.

**40. Events After the Balance Sheet Date**

No circumstances have arisen since the Balance Sheet date which would require adjustments to or disclosure in the Financial Statements other than the following:

- (a) The Board of Directors of the Bank announced its decision to look into the feasibility of merging the Bank with NDB bank subject to the receipt of necessary regulatory and shareholder approvals.
- (b) The Board of Directors of the Bank, at a meeting held on January 31, 2007, recommended a rights issue of ordinary shares on the basis of three new ordinary shares for each ten existing shares to be followed by a Scrip Issue of ordinary shares on the basis of one ordinary share for every three ordinary shares on the enhanced share capital consequent to the Rights Issue.
- (c) The Bank disposed its investment in Commercial Fund Management (Pvt) Ltd., an Associate Company of the Bank on January 23, 2007.

## Income Statement

For the year ended December 31,	Bank			Group		
	2006 US\$ '000	2005 US\$ '000	Change %	2006 US\$ '000	2005 US\$ '000	Change %
<b>Income</b>	<b>227,624</b>	157,809	44.24	<b>227,460</b>	159,041	43.02
Interest income	<b>181,691</b>	127,758	42.21	<b>181,742</b>	130,306	39.47
Less: Interest expenses	<b>111,206</b>	70,830	57.00	<b>111,113</b>	73,108	51.98
Net interest income	<b>70,485</b>	56,928	23.81	<b>70,629</b>	57,198	23.48
Foreign exchange profit	<b>13,386</b>	5,753	132.68	<b>13,386</b>	5,753	132.68
Fee and commission income	<b>18,710</b>	17,249	8.47	<b>18,709</b>	17,248	8.47
Other income	<b>13,837</b>	7,049	96.30	<b>13,623</b>	5,734	137.58
	<b>116,418</b>	86,979	33.85	<b>116,347</b>	85,933	35.39
Less: Operating expenses						
Personnel costs	<b>23,811</b>	20,860	14.15	<b>23,872</b>	21,014	13.60
Premises, equipment and establishment expenses	<b>13,046</b>	11,406	14.38	<b>12,875</b>	11,237	14.58
Provision for staff retirement benefits	<b>16,873</b>	2,313	629.49	<b>16,873</b>	2,313	629.49
Loan losses and provisions	<b>6,094</b>	4,066	49.88	<b>6,094</b>	4,066	49.88
Other overhead expenses	<b>17,398</b>	12,635	37.70	<b>17,017</b>	12,334	37.97
	<b>77,222</b>	51,280	50.59	<b>76,731</b>	50,964	50.56
Profit from operations	<b>39,196</b>	35,699	9.80	<b>39,616</b>	34,969	13.29
Add/(Less): Share of profit/(Loss) before tax of Associate Companies	-	-	-	<b>581</b>	985	(41.02)
<b>Profit before taxation</b>	<b>39,196</b>	35,699	9.80	<b>40,197</b>	35,954	11.80
Less: Provision for taxation	<b>20,474</b>	12,524	63.48	<b>20,919</b>	12,840	62.92
<b>Profit after taxation</b>	<b>18,722</b>	23,175	(19.21)	<b>19,278</b>	23,114	(16.60)
Attributable to:						
Equityholders of the parent	-	-	-	<b>19,262</b>	23,098	(16.61)
Minority Interest	-	-	-	<b>16</b>	16	-
	-	-	-	<b>19,278</b>	23,114	(16.60)
Basic Earnings per Ordinary Share	<b>0.12</b>	0.15	(20.00)	<b>0.12</b>	0.15	(20.00)
Diluted Earnings per Ordinary Share	<b>0.12</b>	0.14	(14.29)	<b>0.12</b>	0.14	(14.29)
Dividend per Ordinary Share	<b>0.05</b>	0.04	25.00	<b>0.05</b>	0.04	25.00

Exchange Rate of 1 US Dollar was Rs. 107.50 as at 31.12.2006 (Rs. 102.02 as at 31.12.2005).

## US DOLLAR ACCOUNTS

The Income Statement and the Balance Sheet given on pages 156 and 157 are solely for the convenience of shareholders, investors, bankers and other users of Financial Statements and do not form part of the Financial Statements.

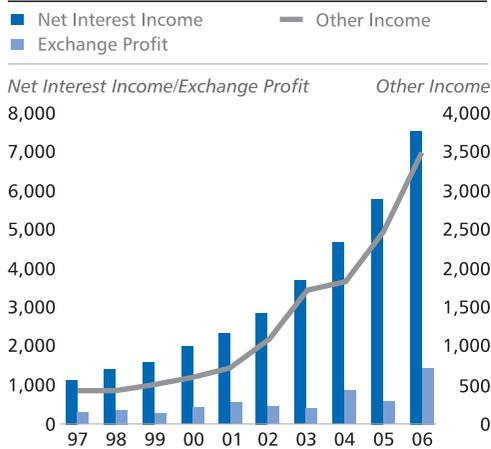
As at December 31,	Bank			Group		
	2006 US\$ '000	2005 US\$ '000	Change %	2006 US\$ '000	2005 US\$ '000	Change %
<b>ASSETS</b>						
Cash and short-term funds	127,802	182,933	(30.14)	127,734	182,874	(30.15)
Balances with Central Banks	116,964	88,661	31.92	116,964	88,661	31.92
Government Treasury Bills and Bonds	112,003	111,842	0.14	113,691	114,345	(0.57)
Commercial paper	3,933	3,995	(1.55)	3,933	3,995	(1.55)
Securities purchased under re-sale agreements	42,726	7,921	439.40	42,726	7,921	439.40
Dealing securities	1,348	1,786	(24.52)	1,348	1,786	(24.52)
Investments held for sale	2,032	-	-	3,733	-	-
Investments held to maturity	12,965	30,302	(57.21)	12,966	30,303	(57.21)
Treasury Bonds maturing after one year	186,278	96,143	93.75	186,278	96,143	93.75
Bills of Exchange	30,588	27,351	11.84	30,588	27,351	11.84
Loans & advances	1,281,171	1,067,283	20.04	1,281,118	1,067,280	20.04
Lease receivable within one year	28,237	24,350	15.96	27,968	24,115	15.98
Lease receivable from one to five years	60,141	45,052	33.49	59,512	44,471	33.82
Lease receivable after five years	162	78	107.69	162	78	107.69
	<u>2,006,350</u>	<u>1,687,697</u>	18.88	<u>2,008,721</u>	<u>1,689,323</u>	18.91
Investments in associate companies	412	1,050	(60.76)	381	2,772	(86.26)
Investments in subsidiary companies	4,034	4,251	(5.10)	-	-	-
Interest and fees receivable	15,246	11,602	31.41	15,246	11,749	29.76
Other assets	26,008	29,328	(11.32)	26,447	28,621	(7.60)
Property, Plant & Equipment	29,928	29,723	0.69	31,977	31,739	0.75
Intangible assets	1,503	1,470	2.24	1,514	1,481	2.23
<b>Total Assets</b>	<u><b>2,083,481</b></u>	<u>1,765,121</u>	18.04	<u><b>2,084,286</b></u>	<u>1,765,685</u>	18.04
<b>LIABILITIES</b>						
Deposits from customers	1,466,363	1,250,748	17.24	1,465,412	1,249,664	17.26
Dividends payable	1,047	2,258	(53.63)	1,047	2,258	(53.63)
Borrowings	176,224	131,220	34.30	176,224	131,220	34.30
Securities sold under re-purchase agreements	133,302	111,637	19.41	133,182	111,607	19.33
Other liabilities	78,177	59,948	30.41	78,159	59,880	30.53
Tax payable	13,449	8,016	67.78	13,211	7,687	71.86
Deferred taxation	5,400	2,099	157.27	5,813	2,229	160.79
Debentures	62,144	44,633	39.23	62,144	44,633	39.23
	<u>1,936,106</u>	<u>1,610,559</u>	20.21	<u>1,935,192</u>	<u>1,609,178</u>	20.26
<b>SHAREHOLDERS' FUNDS</b>						
Share capital	22,588	32,615	(30.74)	22,588	32,615	(30.74)
Statutory Reserve Fund	13,288	13,929	(4.60)	13,296	13,937	(4.60)
Reserves	111,499	108,018	3.22	113,107	109,825	2.99
Shareholders' funds	<u>147,375</u>	<u>154,562</u>	(4.65)	<u>148,991</u>	<u>156,377</u>	(4.72)
Minority Interest	-	-	-	103	130	(20.77)
Total shareholders' funds and Minority interest	<u>147,375</u>	<u>154,562</u>	(4.65)	<u>149,094</u>	<u>156,507</u>	(4.74)
Total liabilities, shareholders' funds and minority interest	<u>2,083,481</u>	<u>1,765,121</u>	18.04	<u>2,084,286</u>	<u>1,765,685</u>	18.04
Commitments and contingencies	<u>498,827</u>	<u>462,203</u>	7.92	<u>498,827</u>	<u>462,203</u>	7.92
Net Assets Value per Ordinary Share (US \$)	<u>0.97</u>	<u>0.95</u>	2.11	<u>0.98</u>	<u>0.96</u>	2.08

Exchange Rate of 1 US Dollar was Rs.107.50 as at 31.12.2006 (Rs. 102.02 as at 31.12.2005).

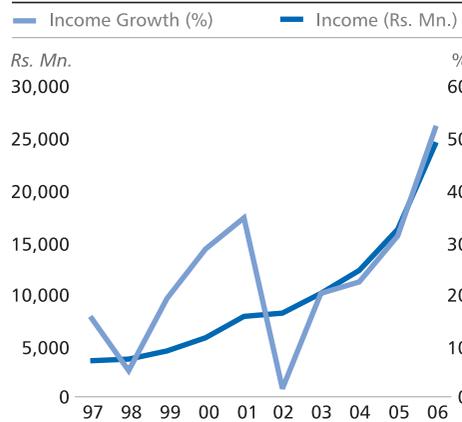
## Subsidiary/Associate Companies

	BANK'S INTEREST	PRINCIPAL ACTIVITY	DIRECTORS		2006 Rs. mn.	2005 Rs. mn.
<b>Subsidiary Companies</b>						
<b>Commercial Bank Primary Dealer Ltd.</b> 'Commercial House', 21, Bristol Street, Colombo 1. Tel: 2445010-15, 2336700, 2328193-5, 2332319 Incorporated on October 18, 1999 (Ceased operations on September 30, 2005)	100.0%	Primary Dealer for Government Securities	M.J.C. Amarasuriya ( <i>Chairman</i> ) B.R.L. Fernando A.L. Gooneratne A.N. Fonseka G.L.H. Premaratne R. Samaranyake W.M.R.S. Dias D.S. Weeraturunge L.W.P. Indrajith ( <i>Company Secretary</i> )	Total assets Net assets Profit before tax Profit after tax Dividend rate (%)	<b>214.929</b> <b>207.577</b> <b>19.325</b> <b>12.637</b> -	308.623 301.440 12.581 47.154 71%
<b>ONEzero Co. Ltd.</b> 'Commercial House', 21, Bristol Street, Colombo 1. Tel: 2430420 Incorporated on February 17, 2003	100.0%	Provision of IT Related Services	M.J.C. Amarasuriya ( <i>Chairman</i> ) A.N. Fonseka A.L. Gooneratne G.L.H. Premaratne R. Samaranyake W.M.R.S. Dias M.D.A. Peiris S.D. Bandaranayake M.P. Dharmasiri ( <i>Company Secretary</i> )	Total assets Net assets Profit before tax Profit after tax Dividend rate (%)	<b>30.083</b> <b>24.242</b> <b>7.029</b> <b>6.984</b> -	23.196 17.257 11.989 11.989 -
<b>X-pertise Ltd.</b> No. 1, Union Place, Colombo 2. Tel: 2305280, 2305282 Incorporated on October 6, 2004 (Operations commenced in 2005)	100.0%	Training & Development of Human Resources	M.J.C. Amarasuriya ( <i>Chairman</i> ) A.L. Gooneratne G.L.H. Premaratne R. Samaranyake W.M.R.S. Dias M.D.A. Peiris Mrs. Sarojini Dunuwille ( <i>Company Secretary</i> )	Total assets Net assets Profit before tax Profit after tax Dividend rate (%)	<b>7.703</b> <b>4.751</b> <b>1.797</b> <b>1.168</b> -	6.842 3.583 (0.514) (0.705) -
<b>Commercial Development Co. Ltd.</b> 'Commercial House', 21, Bristol Street, Colombo 1. Tel: 2447300 Incorporated on March 14, 1980	94.55%	Property Development	M.T.L. Fernando ( <i>Chairman</i> ) A.L. Gooneratne Dr. H.S. Wanasinghe M.A. Pemasiri G.L.H. Premaratne L.W.P. Indrajith ( <i>Company Secretary</i> )	Total assets Net assets Profit before tax Profit after tax Dividend rate (%)	<b>391.717</b> <b>202.253</b> <b>55.145</b> <b>31.101</b> <b>10%</b>	368.624 214.352 47.813 30.110 26%
<b>Associate Companies</b>						
<b>Commercial Fund Management (Pvt.) Ltd.</b> 108 A, 1/1, Maya Avenue, Colombo 6. Tel: 2506347, 5373747 Incorporated on January 20, 1992 (Disposed on January 23, 2007)	50.0%	Fund Management	M.J.C. Amarasuriya ( <i>Chairman</i> ) H.D.S. Amarasuriya A.L. Gooneratne R. Melville R. Hill E.A.D. Perera ( <i>Alternate</i> ) Mrs. R.R. Dunuwille ( <i>Company Secretary</i> )	Total assets Net assets Profit before tax Profit after tax Dividend rate (%)	<b>45.615</b> <b>41.998</b> <b>10.642</b> <b>6.640</b> <b>5%</b>	41.595 37.508 11.055 7.179 -
<b>Commercial Leasing Co. Ltd.</b> 68, Baudhaloka Mawatha, Colombo 4. Tel: 4526526 Incorporated on April 22, 1988	30.0%	Leasing, Factoring, Hire Purchase and Hiring of Vehicles	H.D.S. Amarasuriya ( <i>Chairman</i> ) M.J.C. Amarasuriya A.L. Gooneratne M.P. Jayawardena K.K. Shah P.R. Saldin H.A. Peiris ( <i>Alternate</i> ) Nihal A. Rodrigo ( <i>Company Secretary</i> )	Total assets Net assets Profit before tax Profit after tax Dividend rate (%)	<b>7,745.782</b> <b>1,037.783</b> <b>368.115</b> <b>268.101</b> <b>20%</b>	5,927.011 605.603 313.433 208.893 45%
<b>Equity Investments Lanka Ltd.</b> 108 A, 1st Floor, Maya Avenue, Colombo 6. Tel: 5373745, 2507605-6 Incorporated on August 08, 1990	22.92%	Venture Capital Financing	M.J.C. Amarasuriya ( <i>Chairman</i> ) H.D.S. Amarasuriya S.T. Nagendra A.L. Gooneratne Deshabandu S.E. Captain YAM. T.T.S.I.I.T. Ja'afar E.A.D. Perera ( <i>Alternate</i> ) Mrs. R.R. Dunuwille ( <i>Company Secretary</i> )	Total assets Net assets Profit before tax Profit after tax Dividend rate (%)	<b>184.940</b> <b>178.722</b> <b>10.671</b> <b>9.929</b> -	182.409 174.175 5.521 5.420 3%

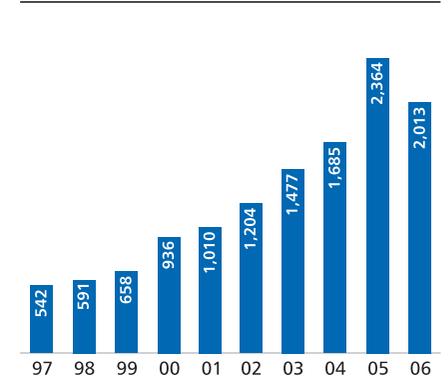
**Net Interest Income, Exchange Profit, Fees & Other Income (Rs. Mn.)**



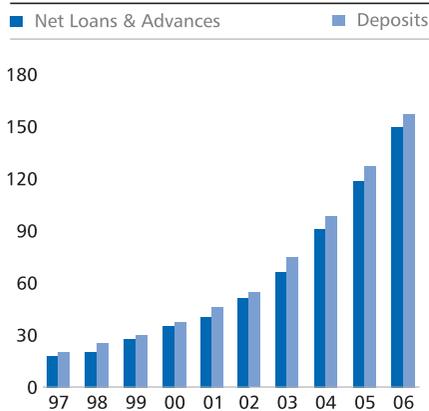
**Income & Income Growth**



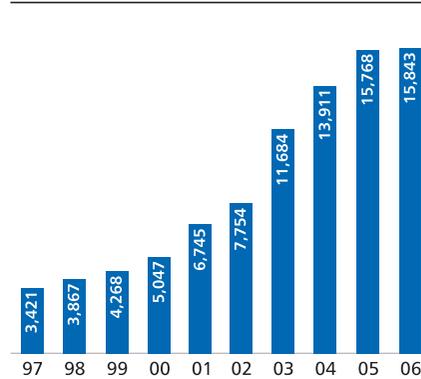
**Profit after Taxation (Rs. Mn.)**



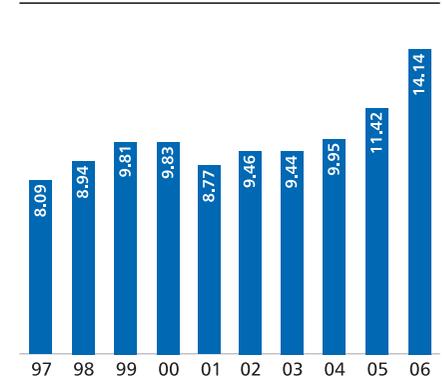
**Growth in Business Volumes (Rs. Bn.)**



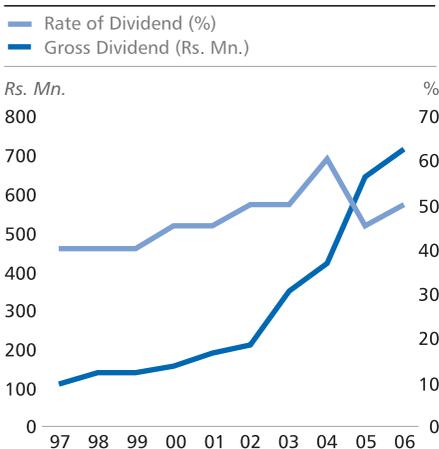
**Ordinary Shareholders' Funds (Rs. Mn.)**



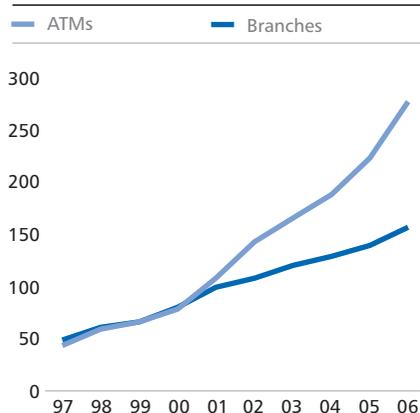
**Total Assets to Shareholders' Funds (Times)**



**Gross Dividend to Ordinary Shareholders & Rate of Dividend**



**Branches & ATM Expansion (No.)**



## Decade at a Glance

### Bank

(Rs. Mn.)	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	CAGR %
<i>For the year ended December 31</i>											
<b>Operating Results</b>											
Income	3,781	3,979	4,744	6,096	8,203	8,364	10,059	12,290	16,100	<b>24,470</b>	21.95
Interest income	2,876	3,031	3,762	4,796	6,510	6,613	7,931	9,584	13,034	<b>19,532</b>	
Interest expenses	(1,723)	(1,605)	(2,158)	(2,776)	(4,174)	(3,747)	(4,218)	(4,878)	(7,226)	<b>(11,955)</b>	
Foreign Exchange profit	320	362	274	421	563	464	397	874	587	<b>1,439</b>	
Commission & other income	440	440	517	600	732	1,097	1,731	1,832	2,479	<b>3,499</b>	
Operating expenses & provisions	(1,261)	(1,459)	(1,586)	(1,891)	(2,306)	(2,902)	(3,887)	(4,908)	(5,232)	<b>(8,301)</b>	
Profit before income tax	652	769	809	1,150	1,325	1,525	1,954	2,504	3,642	<b>4,214</b>	21.93
Income tax on profit	(110)	(178)	(151)	(214)	(315)	(321)	(477)	(819)	(1,278)	<b>(2,201)</b>	
Net profit for the year	542	591	658	936	1,010	1,204	1,477	1,685	2,364	<b>2,013</b>	16.61
<i>As at December 31</i>											
<b>Assets</b>											
Cash and short-term funds	4,639	8,440	4,050	5,456	4,272	1,835	9,002	12,136	18,663	<b>13,739</b>	
Balances with Central Banks	1,938	1,840	2,644	2,583	3,091	3,244	5,233	6,320	9,045	<b>12,574</b>	
Government Treasury Bills and Bonds	–	409	2,614	1,067	649	8,654	15,930	5,522	11,410	<b>12,040</b>	
Commercial paper	–	–	745	331	1,170	1,080	546	560	408	<b>423</b>	
Securities purchased under re-sale agreements	–	70	–	–	1,064	832	6,184	399	808	<b>4,593</b>	
Dealing Securities & Investments held for sale	–	–	–	–	–	–	–	110	182	<b>363</b>	
Investments held to maturity	658	409	300	208	462	905	2,006	2,340	3,091	<b>1,394</b>	
Treasury Bonds maturing after one year	–	–	959	382	4,658	782	600	14,378	9,808	<b>20,025</b>	
Bills of Exchange	2,074	1,597	1,873	2,331	2,368	2,552	2,495	2,799	2,790	<b>3,288</b>	
Loans and advances	15,690	18,312	24,787	31,703	36,730	47,350	60,585	82,605	108,884	<b>137,726</b>	25.34
Lease receivable	489	730	1,047	1,263	1,519	1,921	3,364	5,317	7,088	<b>9,518</b>	
	25,488	31,807	39,019	45,324	55,983	69,155	105,945	132,486	172,177	<b>215,683</b>	
Investments in associate companies	128	78	78	78	78	78	78	109	107	<b>44</b>	
Investments in subsidiary companies	274	274	274	424	424	424	429	429	434	<b>434</b>	
Other assets	972	1,368	1,253	2,478	1,251	2,149	2,167	2,553	4,177	<b>4,434</b>	
Property, Plant & Equipment and Intangible Assets	797	1,059	1,263	1,306	1,410	1,546	1,661	2,896	3,182	<b>3,379</b>	
<b>TOTAL ASSETS</b>	<b>27,659</b>	<b>34,586</b>	<b>41,887</b>	<b>49,610</b>	<b>59,146</b>	<b>73,352</b>	<b>110,280</b>	<b>138,473</b>	<b>180,077</b>	<b>223,974</b>	24.35
<b>Liabilities</b>											
Deposits from customers	20,156	25,274	30,128	37,523	46,306	54,585	75,185	98,730	127,601	<b>157,634</b>	25.23
Dividends Payable	75	98	98	108	163	118	190	230	230	<b>113</b>	
Borrowings	1,321	1,124	1,350	2,317	1,862	4,200	5,406	9,090	13,387	<b>18,944</b>	
Securities sold under re-purchase agreements	1,468	2,130	3,371	1,430	228	1,938	10,580	9,050	11,389	<b>14,330</b>	
Other liabilities & Deferred Taxation	1,226	1,594	2,168	2,643	3,263	4,218	4,843	3,735	6,331	<b>8,984</b>	
Tax Payable	(8)	(1)	4	42	79	39	148	483	818	<b>1,446</b>	
Debentures	–	500	500	500	500	500	2,244	3,244	4,553	<b>6,680</b>	
	24,238	30,719	37,619	44,563	52,401	65,598	98,596	124,562	164,310	<b>208,131</b>	
<b>Shareholders' Funds</b>											
Share capital	268	348 <sup>†</sup>	348	348	1,324 <sup>-1</sup>	1,324	2,603 <sup>*•</sup>	2,603	3,327 <sup>**</sup>	<b>2,428 <sup>***</sup></b>	
Reserve fund	1,009	1,009	1,009	1,009	1,009	1,009	1,009	1,009	1,421	<b>1,429</b>	
Reserves	2,144	2,510	2,911	3,690	4,412	5,421	8,072	10,299	11,020	<b>11,986</b>	
<b>TOTAL LIABILITIES &amp; SHAREHOLDERS' FUNDS</b>	<b>27,659</b>	<b>34,586</b>	<b>41,887</b>	<b>49,610</b>	<b>59,146</b>	<b>73,352</b>	<b>110,280</b>	<b>138,473</b>	<b>180,077</b>	<b>223,974</b>	24.35
Commitments and contingencies	13,768	14,612	15,445	17,880	19,749	24,082	38,158	43,942	47,154	<b>53,624</b>	

CAGR - Compounded Annual Growth Rate over the last decade

<b>Bank</b>	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006
<b>Ratios</b>										
Return on average -										
shareholders' funds (%)	16.80	16.20	16.21	20.09	17.13	16.61	15.20	13.16	15.93	<b>12.73</b>
Income growth (%)	15.71	5.24	19.25	28.49	34.56	1.96	20.26	22.17	31.00	<b>51.99</b>
Return on average assets (%)	2.05	1.90	1.72	2.05	1.86	1.82	1.61	1.35	1.48	<b>1.00</b>
Rate of dividend (%)	40.00	40.00	40.00	45.00	45.00	50.00	50.00	60.00	45.00	<b>50.00</b>
Ordinary share dividend cover (times)	3.90	4.24	4.73	5.91	5.20	5.20	3.70	3.48	3.34	<b>2.54</b>
Gross dividends										
to ordinary shareholders (Rs. Mn.)	107.10	139.30	139.30	156.71	188.06	208.95	348.25	418.10	639.36	<b>714.00</b>
Advances to deposits and										
refinance (%)	88.95	80.42	89.75	91.81	85.51	92.59	86.16	89.52	90.64	<b>92.49</b>
Property, Plant & Equipment to										
shareholders' funds (%)	23.29	27.37	29.72	25.87	20.90	19.93	14.22	20.81	20.75	<b>21.33</b>
Total assets to shareholders'										
funds (times)	8.09	8.94	9.81	9.83	8.77	9.46	9.44	9.95	11.42	<b>14.14</b>
Capital Funds to Liabilities including										
Contingent Liabilities (%)	9.00	8.53	8.04	8.08	9.35	8.65	8.54	8.26	7.46	<b>6.05</b>
Cost/Income Ratio (%)	55.62	56.91	58.66	54.75	55.27	55.46	55.87	56.78	54.28	<b>61.10</b>
Liquid assets to liabilities (%)	25.36	24.97	22.19	27.22	27.72	27.88	23.95	23.17	24.51	<b>22.64</b>
(As specified in the Banking Act										
No. 30 of 1988)										
Group Capital Adequacy (%) Tier I	16.71	15.53	14.90	14.97	15.72	14.94	13.43	10.78	9.68	<b>7.62</b>
Tier I & II	17.63	18.45	17.14	16.62	16.20	15.07	15.46	13.16	12.08	<b>11.58</b>
<b>Information on Ordinary Shares</b>										
Market value of a voting share (Rs.)	150	120	115	93	127	200	144	159.75	135.50	<b>190.00</b>
Basic earnings per share (Rs.)	4	4	5	7	7	8	9	10	15	<b>13</b>
Price earnings ratio (times)	10	7	6	4	5	8	8	8	9	<b>15</b>
Net assets value per share (Rs.)	24	27	30	35	41	48	69	84	98	<b>104</b>
Earnings yield (%)	11	14	16	29	18	13	13	13	11	<b>7</b>
Dividend payout ratio (%)	25	24	21	17	22	18	27	29	30	<b>39</b>
<b>Other Information</b>										
No. of employees	1,889	1,985	1,996	2,067	2,259	2,399	2,648	2,863	3,168	<b>3,415</b>
No. of branches / CSPs / MiniComs/										
Service Points - Sri Lanka	49	61	67	81	100	109	116	125	134	<b>150</b>
No. of branches / booths - Bangladesh	–	–	–	–	–	–	4	4	5	<b>7</b>
No. of Automated Teller Machines	44	60	67	79	109	143	166	188	223	<b>278</b>

+ Scrip issue of three bonus shares for every ten ordinary shares held was made in June 1998.

~ Scrip issue of one bonus share for every five ordinary shares held was made in May 2001.

^ Issue of 13% Cumulative Redeemable Preference Shares of Rs. 10/- each for Rs. 906.555 million was made in August 2001.

\* Scrip issue of one bonus share for every three ordinary shares held was made in May 2003.

▲ Rights issue of one ordinary share for every four ordinary shares held was made in October 2003.

• Issue of 11.25% Cumulative Redeemable Preference Shares of Rs. 10/- each for Rs. 1,000.000 million was made in May 2003.

\*\* Scrip issue of one bonus share for every one ordinary share held was made in June 2005.

\*\*\* Redemption of 13% Cumulative Redeemable Preference Shares in September 2006.

## Share and Debenture Information

### 1. Stock Exchange Listing

The ordinary shares, both voting and non-voting, preference shares, 2003/2008 debentures, December 2006/ December 2011 debentures, December 2006/December 2013 debentures and December 2006/December 2016 debentures, both fixed and floating interest rate of the Bank are listed in the Colombo Stock Exchange. The audited Income Statement for the year ended December 31, 2006 and the audited Balance Sheet of the Bank as at date will be submitted to the Colombo Stock Exchange within three months of the Balance Sheet date.

### 2. Ordinary Shareholders

As at December 31, 2006

#### 2.1 Voting

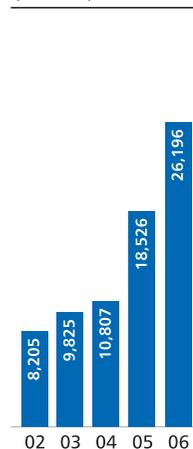
Range of Shareholdings	Resident		Non-Resident		Total		
	No. of Shareholders	No. of Shares	No. of Shareholders	No. of Shares	No. of Shareholders	No. of Shares	%
Up to 500 shares	2,398	420,999	23	3,540	2,421	424,539	0.32
501 - 5,000	2,680	5,384,406	74	164,567	2,754	5,548,973	4.16
5,001 - 10,000	469	3,308,447	21	138,750	490	3,447,197	2.58
10,001 - 20,000	262	3,588,053	5	74,410	267	3,662,463	2.74
20,001 - 30,000	109	2,649,635	2	55,000	111	2,704,635	2.03
30,001 - 40,000	38	1,283,250	-	-	38	1,283,250	0.96
40,001 - 50,000	23	1,030,992	1	50,000	24	1,080,992	0.81
50,001 - 100,000	45	3,123,441	4	241,586	49	3,365,027	2.52
100,001 - 1,000,000	37	9,743,162	9	3,126,000	46	12,869,162	9.64
Over 1,000,000 shares	11	85,257,026	2	13,875,000	13	99,132,026	74.24
	<b>6,072</b>	<b>115,789,411</b>	<b>141</b>	<b>17,728,853</b>	<b>6,213</b>	<b>133,518,264</b>	<b>100.00</b>

There were 6,304 resident and 134 non-resident shareholders as at December 31, 2005.

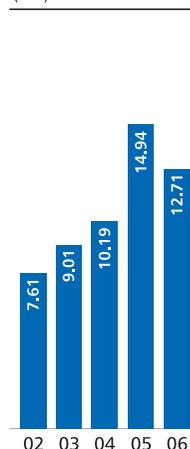
Analysis of Shareholders	December 31, 2006			December 31, 2005		
	No. of Shareholders	Total Holdings	%	No. of Shareholders	Total Holdings	%
Individuals	5,881	29,371,641	22.00	5,800	36,634,561	27.59
Institutions	332	104,146,623	78.00	638	96,145,961	72.41
	<b>6,213</b>	<b>133,518,264</b>	<b>100.00</b>	<b>6,438</b>	<b>132,780,522</b>	<b>100.00</b>

As per the Rule No. 8.7 (h) of the Colombo Stock Exchange, percentage of public holding as at December 31, 2006 was 46.23% (45.93% as at December 31, 2005).

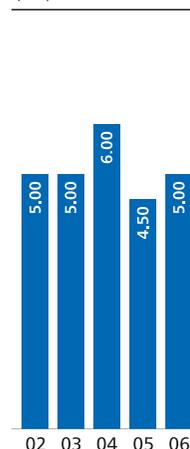
#### Market Capitalisation (Rs. Mn.)



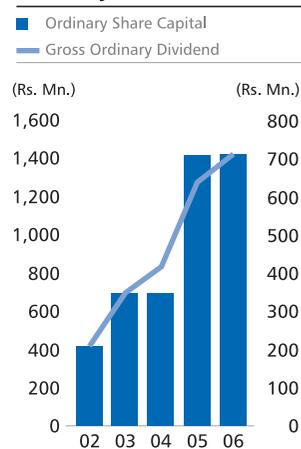
#### Earnings per Share (Rs.)



#### Dividend per Share (Rs.)



#### Ordinary Share Capital & Gross Dividend on Ordinary Shares



## 2.2 Non-Voting

Range of Shareholdings	Resident		Non-Resident		Total		
	No. of Shareholders	No. of Shares	No. of Shareholders	No. of Shares	No. of Shareholders	No. of Shares	%
Up to 500 shares	1,067	221,282	11	1,963	1,078	223,245	2.40
501 - 5,000	900	1,570,343	20	49,668	920	1,620,011	17.42
5,001 - 10,000	117	855,231	5	42,400	122	897,631	9.65
10,001 - 20,000	60	853,117	5	91,500	65	944,617	10.16
20,001 - 30,000	30	692,502	2	48,500	32	741,002	7.97
30,001 - 40,000	18	622,844	-	-	18	622,844	6.70
40,001 - 50,000	9	406,340	1	43,000	10	449,340	4.83
50,001 - 100,000	9	611,062	1	57,400	10	668,462	7.19
100,001 - 1,000,000	9	2,892,508	1	240,800	10	3,133,308	33.68
Over 1,000,000 shares	-	-	-	-	-	-	0.00
	<b>2,219</b>	<b>8,725,229</b>	<b>46</b>	<b>575,231</b>	<b>2,265</b>	<b>9,300,460</b>	<b>100.00</b>

There were 2,368 resident and 42 non-resident shareholders as at December 31, 2005.

Analysis of Shareholders	December 31, 2006			December 31, 2005		
	No. of Shareholders	Total Holdings	%	No. of Shareholders	Total Holdings	%
Individuals	2,125	5,482,010	58.94	2,260	5,749,710	61.82
Institutions	140	3,818,450	41.06	150	3,550,750	38.18
	<b>2,265</b>	<b>9,300,460</b>	<b>100.00</b>	<b>2,410</b>	<b>9,300,460</b>	<b>100.00</b>

As per the Rule No. 8.7 (h) of the Colombo Stock Exchange, percentage of public holding as at December 31, 2006 was 87.95% (87.95% as at December 31, 2005).

## 3. Twenty largest Shareholders as at December 31

## Ordinary Voting Shares

Name of the Shareholder	2006		2005*	
	No. of Shares	%	No. of Shares	%
DFCC Bank	38,706,270	28.99	38,706,270	29.15
HSBC Intl. Nominees Ltd. - SSBT - International Finance Corporation	19,500,000	14.61	19,500,000	14.69
Galleon Deversified Fund Ltd.	7,100,000	5.32	-	-
Sri Lanka Insurance Corporation Ltd. - Life Fund	6,931,620	5.19	6,931,620	5.22
Abdulaziz Mohammed A. Almeshaal	6,775,000	5.07	13,275,000	10.00
Sri Lanka Insurance Corporation Ltd. - General Fund	5,960,240	4.46	5,960,240	4.49
National Savings Bank	3,075,382	2.30	2,694,382	2.03
Distilleries Company of Sri Lanka Ltd.	2,989,970	2.24	2,989,970	2.25
HSBC Intl. Nominees Ltd. - BPSS LUX - Aberdeen Global Asia Pacific Fund	2,952,800	2.21	2,627,000	1.98
Northern Trust Co. S/A Murray Johnstone International Delaware Business Trust	1,545,600	1.16	660,000	0.50
Yonmerrenge Simon Hewage Indra Kumar Silva	1,355,144	1.01	1,158,944	0.87
HSBC Intl. Nominees Ltd. - SSBTL - Aberdeen Asia Smaller Companies Investment Trust XC	1,150,000	0.86	1,150,000	0.87
HSBC Intl. Nominees Ltd. - JPMCB - Scottish ORL SML TR GTI 6018	1,090,000	0.82	1,090,000	0.82
HSBC Intl. Nominees Ltd. - BPSS LUX - Aberdeen - Global - Asian Smaller Company	984,000	0.74	984,000	0.74
HBSC Ltd. - National Equity Fund	880,000	0.66	880,000	0.66
Hatton National Bank Ltd. A/C No.1	825,332	0.62	825,332	0.62
Freudenberg Shipping Agencies Ltd.	775,000	0.58	771,100	0.58
City Properties (Pvt) Ltd.	669,400	0.50	669,400	0.50
HSBC Intl. Nominees Ltd. - HSBC Bank PLC - CMG First State Global Umbrella Fund PLC - CM	500,000	0.37	-	-
Renuka City Hotels Ltd.	449,000	0.34	339,000	0.26
Sub Total	104,214,758	78.05	101,212,258	76.23
Others	29,303,506	21.95	31,568,264	23.77
Total	133,518,264	100.00	132,780,522	100.00

\* Comparative shareholdings as at December 31, 2005 of the twenty largest shareholders as at December 31, 2006.

## Share and Debenture Information

### Ordinary Non-Voting Shares

Name of the Shareholder	2006		2005*	
	No. of Shares	%	No. of Shares	%
Sri Lanka Insurance Corporation Ltd. - General Fund	987,670	10.62	987,670	10.62
JB Cocoshell (Pvt) Ltd.	488,600	5.25	185,800	2.00
Akbar Brothers Ltd A/C No. 1	456,416	4.91	381,316	4.10
Beta Holdings Ltd	240,800	2.59	161,900	1.74
The Associated Newspapers of Ceylon Ltd.	208,262	2.24	208,262	2.24
The Gilpin Fund Ltd.	200,000	2.15	200,000	2.15
M.J.F. Exports Ltd.	160,776	1.73	160,776	1.73
M.S.H. Packaging Industries Ltd.	159,500	1.72	190,300	2.04
Jayampathi Divale Bandaranayake	126,352	1.36	86,352	0.93
Mahendra Jayanthipal Chandima Amarasuriya	104,932	1.13	104,932	1.13
Alpex Marine (Pvt) Ltd.	100,000	1.08	100,000	1.08
Mohamed Faizer Hashim	90,730	0.98	4,030	0.04
Jayalath Githal De Mel	76,950	0.83	64,750	0.69
Ananda Krishnakumar Abeytunga Jayawardene	72,724	0.78	70,724	0.76
Renuka Holdings Ltd.	60,014	0.65	60,014	0.65
Harnam Singh Mantha Singh	57,400	0.62	57,400	0.62
HSBC Ltd. o/a NAMAL Growth Fund	55,000	0.59	55,000	0.59
Employees' Trust Fund Board	54,564	0.59	50,364	0.54
William Ryan Herbert Perera	50,580	0.54	43,580	0.47
Deepak Naraindas Hundlani	50,500	0.54	78,000	0.84
Sub Total	3,801,770	40.89	3,251,170	34.96
Others	5,498,690	59.11	6,049,290	65.04
Total	9,300,460	100.00	9,300,460	100.00

\* Comparative shareholdings as at December 31, 2005 of the twenty largest shareholders as at December 31, 2006.

### 4. Market Value of Shares

	2006 Rs.	2005 Rs.
<b>Ordinary Voting Shares</b>		
Highest	192.50	269.00
Lowest	123.00	120.00
Year end	190.00	135.50
<b>Ordinary Non-Voting Shares</b>		
Highest	90.00	160.00
Lowest	54.00	51.00
Year end	89.00	57.50
<b>13% Cumulative Redeemable Preference Shares (Redeemed on September 20, 2006)</b>		
Highest	9.75	11.25
Lowest	9.25	9.00
Year end	9.50	9.75
	(As at 08.08.06)	(As at 19.12.05)
<b>11.25% Cumulative Redeemable Preference Shares</b>		
Highest	9.25	11.25
Lowest	7.00	9.00
Year end	9.25	9.75
	(As at 05.10.06)	(As at 06.12.05)

## 5. Market Capitalisation

Market capitalisation of the Bank which is the number of ordinary shares in issue multiplied by the market value of a share was Rs. 26.196 billion as at December 31, 2006 (Rs. 18.526 billion as at December 31, 2005). This accounted for 3.04% (3.07% in 2005) of the total Market Capitalisation of the Colombo Stock Exchange and ranked number 5 (number 4 in 2005) among the listed public companies. Commercial Bank ranked number 9 in terms of the value of the ordinary voting shares traded on the Colombo Stock Exchange (Number 5 in 2005).

## 6. Dividends

On Ordinary Shares	2006	2005
Interim paid	15%	15%
Final proposed/paid	35%	30%
Total	50%	45%

On 13% and 11.25% Cumulative Redeemable Preference Shares - dividends were paid on September 20, 2006 (date of redemption) and on January 3, 2007 respectively for the period/year ended December 31, 2006 (on January 3, 2006 for the year ended December 31, 2005).

## 7. Share Trading

Ordinary Shares	2006	2005
No. of transactions	9,578	14,790
No. of shares traded	20,015,500	31,784,500
Value of shares traded (Rs.)	3,114,229,375	4,667,195,475
<b>13% Cumulative Redeemable Preference Shares (Redeemed on September 20, 2006)</b>		
No. of transactions	11	11
No. of shares traded	70,200	33,300
Value of shares traded (Rs.)	661,925	317,425
<b>11.25% Cumulative Redeemable Preference Shares</b>		
No. of transactions	3	21
No. of shares traded	15,000	151,800
Value of shares traded (Rs.)	125,000	1,459,875

## 8. Financial Ratios

Key financial ratios are given in the 'Decade at a Glance' on page 160.

## 9. Investments

The details of investments in shares of Subsidiary/Associate Companies are given on pages 132-134.

### Share Trading (No.)



## Share and Debenture Information

### 10. Information on Debentures

Debenture categories	CSE Listing	Interest payable frequency	Market values		
			Highest Rs.	Lowest Rs.	Year End Rs.
<b>Fixed rate</b>					
2003/2008 - 10.00% p.a.	Listed	Quarterly	1,000	1,000	1,000 (as at 13.09.06)
			(970)	(970)	(970) (as at 05.10.05)
2005/2010 - 12.00% p.a.	Not listed	Annually	-	-	-
			-	-	-
May 2006/May 2011 - 12.00% p.a.	Not listed	Annually	-	-	-
May 2006/May 2016 - 13.25% p.a.	Not listed	Annually	-	-	-
Dec. 2006/Dec. 2011 - 13.50% p.a.	Listed	Annually	Not traded during the year		
Dec. 2006/Dec. 2013 - 13.75% p.a.	Listed	Annually	Not traded during the year		
Dec. 2006/Dec. 2016 - 14.00% p.a.	Listed	Annually	Not traded during the year		
<b>Floating rate</b>					
2003/2008 - 3 Months TB rate (Net) + 2% p.a.	Listed	Quarterly	Not traded during the year		
			(971)	(971)	(971)
2004/2009 - 3 Months TB rate (Net) + 2% p.a.	Not listed	Quarterly	-	-	(as at 05.10.05)
			-	-	-
2005/2010 - 3 Months TB rate (Net) + 2% p.a.	Not listed	Quarterly	-	-	-
			-	-	-
2005/2010 -3 Months TB rate (Gross) + 1% p.a.	Not listed	Quarterly	-	-	-
			-	-	-
May 2006/May 2011 - 3 Months TB rate (Net) + 2% p.a.	Not listed	Quarterly	-	-	-
May 2006/May 2011 - 3 Months TB rate (Gross) + 1% p.a.	Not listed	Quarterly	-	-	-
Dec. 2006/Dec. 2011 - 12 Months TB rate (Gross) + 1% p.a.	Listed	Annually	Not traded during the year		
Dec. 2006/Dec. 2013 - 12 Months TB rate (Gross) + 1% p.a.	Listed	Annually	Not traded during the year		
Dec. 2006/Dec. 2016 - 12 Months TB rate (Gross) + 1% p.a.	Listed	Annually	Not traded during the year		

(The comparative figures for 2005 are given in brackets)

3 Months TB rate (Gross) - three months Treasury Bill rate before 10% Withholding Tax as published by the Central Bank of Sri Lanka immediately prior to the commencement of each interest period.

3 Months TB rate (Net) - three months Treasury Bill rate after 10% Withholding Tax as published by the Central Bank of Sri Lanka immediately prior to the commencement of each interest period.

12 Months TB rate (Gross) - twelve months Treasury Bill rate before 10% Withholding Tax as published by the Central Bank of Sri Lanka immediately prior to the commencement of each interest period.

## Share and Debenture Information

Interest Rates		Interest rate of Comparable Government Security %	Other Ratios	
Coupon Rate %	Effective Annual Yield %		Interest Yield %	Yield to Maturity %
10.00	10.38	13.50	10.38 (as at 13.09.06)	9.80 (as at 13.09.06)
(10.00)	(10.38)	(11.05)	(10.70) (as at 05.10.05)	(12.68) (as at 05.10.05)
12.00	12.00	13.75	–	–
(12.00)	(12.00)	(11.25)	–	–
12.00	12.00	13.75	–	–
13.25	13.25	(Indicative) 14.25	–	–
13.50	13.50	13.75	–	–
13.75	13.75	(Indicative) 14.00	–	–
14.00	14.00	(Indicative) 14.25	–	–
12.53	12.79	13.50	11.10 (as at 05.10.05)	13.05 (as at 05.10.05)
(11.62)	(10.77)	(11.05)	(11.10)	(13.05)
12.53	12.79	13.65	–	–
(11.62)	(10.77)	(11.20)	–	–
12.53	12.79	13.75	–	–
(11.65)	(11.65)	(11.25)	–	–
12.70	12.94	13.75	–	–
(11.73)	(11.73)	(11.25)	–	–
12.53	12.82	13.75	–	–
12.70	12.97	13.75	–	–
15.19	15.19	13.75	–	–
15.19	15.19	(Indicative) 14.00	–	–
15.19	15.19	(Indicative) 14.25	–	–

### Other Ratios

	2006	2005
Debt Equity Ratio (%)	<b>46.58</b>	33.89
Interest Cover (Times)	<b>7.57</b>	10.82
Quick Assets Ratio (%)	<b>22.64</b>	24.51

## Eighty-Six Years Tradition

<b>1920</b>	The Eastern Bank Ltd. (EBL) opens a branch in Chatham Street.
<b>1957</b>	The share capital of EBL is acquired by Chartered Bank.
<b>1969</b>	The Commercial Bank of Ceylon Ltd. incorporated with EBL holding 40% of its equity.
<b>1971</b>	The business of the EBL is taken over by the Chartered Bank.
<b>1973</b>	The Galle, Jaffna and Kandy branches of the Mercantile Bank Ltd. are acquired by the Bank.
<b>1979</b>	The Foreign Currency Banking Unit is formed.
<b>1980</b>	Commercial Development Company Ltd. is incorporated to construct a Headquarters for the Bank with a 40% equity participation.
<b>1984</b>	The Headquarters of the Bank is shifted to "Commercial House", 21, Bristol Street, Colombo 1.
<b>1985</b>	The Foreign Department is elevated to the status of a fully-fledged branch. This move completed the reorganisation process whereby three independent offices representing the City Office, the Foreign Branch and the Head Office were created by segregating the different operations.
<b>1987</b>	EBL changes its name to Standard Chartered (UK) Holdings Ltd.
<b>1988</b>	An associate company, Commercial Leasing Company Ltd. is formed.
<b>1992</b>	The Bank sponsors a Fund Management Company, Commercial Fund Management (Pvt.) Ltd. for the purpose of operating unit trusts. The first unit trust launched in March 1992. The Bank enjoys a 50% equity participation in this company.
<b>1993</b>	Introduction of the Core Banking Software-International Comprehensive Banking System (ICBS) linking nine metropolitan branches.
<b>1997</b>	Standard Chartered Bank sells its 40% stake in the Bank.
<b>1998</b>	365 day branch at Colombo 7 Branch is opened. All branches except Jaffna are linked to the ICBS.
<b>1999</b>	Banking and supermarketing are combined by opening the first "MiniCom" at the Staples Street Cargills Food City outlet. Rated as the Best Bank in Sri Lanka by "Global Finance".
<b>2000</b>	Internet Banking is launched. Rated as the Best Bank in Sri Lanka by "Global Finance" for the second consecutive year.
<b>2001</b>	Receives SL AA+ rating from Fitch Ratings Lanka Ltd. Rated as the Best Bank in Sri Lanka by "Global Finance" for the third consecutive year. Selected as the Bank of the Year by "The Banker" Magazine.
<b>2002</b>	Selected as the No. 1 Corporate in Sri Lanka by "Business Today" Magazine. Rated as the best Bank in Sri Lanka by "Global Finance" for the fourth consecutive year. Selected as the Bank of the Year by "The Banker" Magazine for the second consecutive year. Fitch Ratings Lanka Ltd. upholds the SL AA+ rating in their annual review. Winner of the overall National Award for HRM - 2002. South Asian Federation of Accountants (SAFA) ranks the Bank's Annual Report for 2001 to be the first in the Financial Sector.

**2003** Rated as the Best Bank in Sri Lanka by "Global Finance" for the fifth consecutive year. Selected as the Bank of the Year by "The Banker" Magazine for the third consecutive year. Fitch Ratings Lanka Ltd. upholds the SL AA+ rating in their annual review. SAFA rates Annual Report 2002 as the Best Presented Accounts of the Financial Sector. The Institute of Chartered Accountants of Sri Lanka (ICASL) ranks the Annual Report 2001 of the Bank as the Overall Winner, the Winner of the Financial Sector and Winner of Corporate Governance Disclosure Award. The operations of Credit Agricole Indosuez in Bangladesh is taken over. The first service point at Arpico Super Centre was opened at Dehiwela.

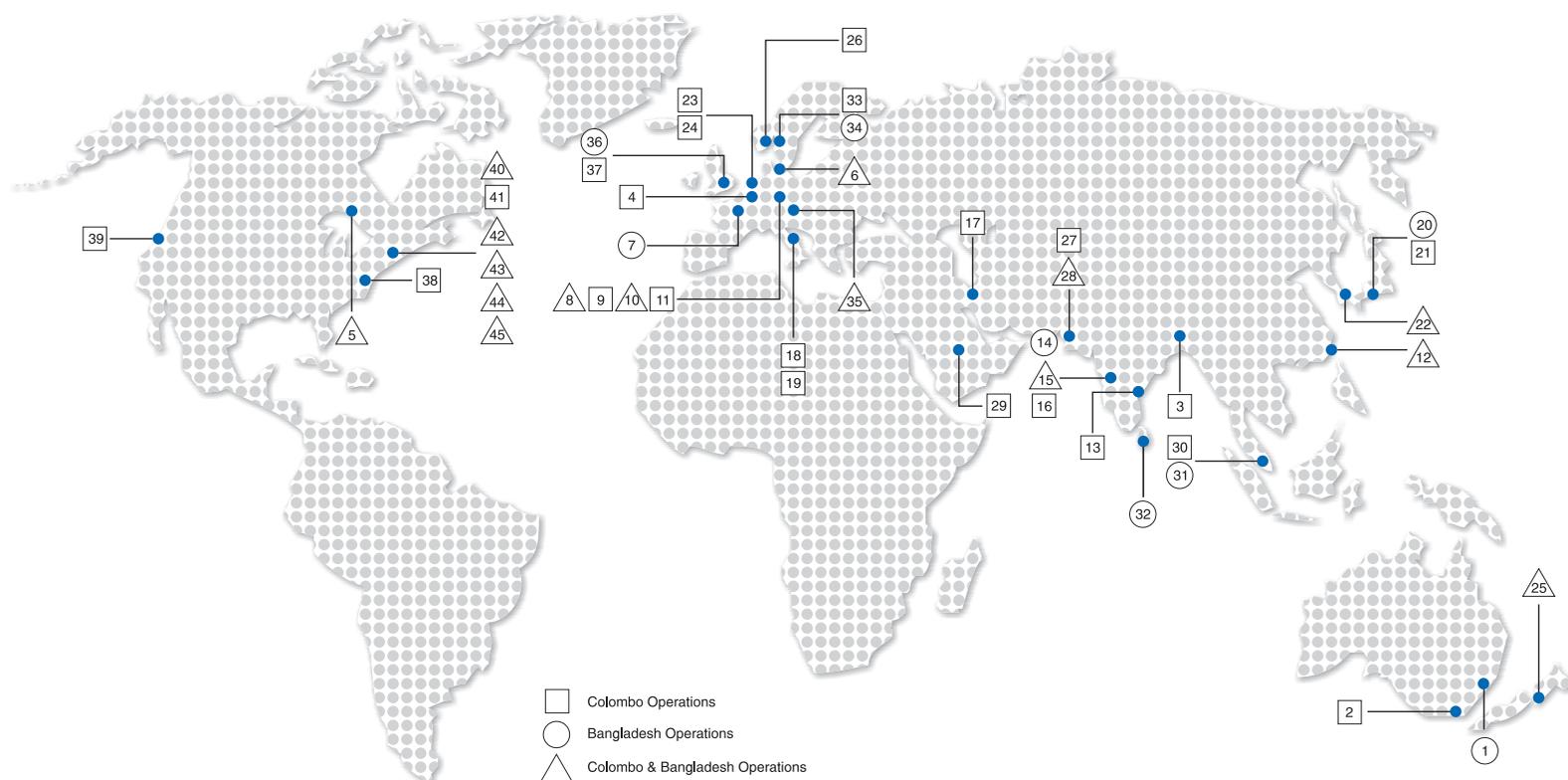
**2004** Rated as the Best Bank in Sri Lanka by "Global Finance" for the sixth consecutive year. Selected as the Bank of the Year by "The Banker" Magazine for the fourth consecutive year. Fitch Ratings Lanka Ltd. upholds the AA+ (sri) rating in their annual review. SAFA rates Annual Reports 2002 and 2003 as the Best Presented Accounts of the Financial Sector. The ICASL ranks the Annual Reports 2002 and 2003 of the Bank as follows:

Award	2003	2002
Overall	Winner	Winner
Banking Sector	Winner	Winner
Corporate Governance Disclosure	Joint 1st Runners up	Winner
Corporate Social Responsibility	Joint 1st Runners up	Joint 2nd Runners up

Overall HRM winner in the Large Service Sector and winner - most innovative HR Practices. Commercial Bank Social Responsibility Trust was set up in September.

**2005** Rated as the Best Bank in Sri Lanka by "Global Finance" for the seventh consecutive year. Selected as the Bank of the Year by "The Banker" Magazine for the fifth consecutive year. Fitch Ratings Lanka Ltd. upholds the AA+ (sri) rating in their annual review. SAFA rates Annual Report 2004 as the Overall Winner and the Best Presented Accounts of the Financial Sector. The ICASL ranks the Annual Report 2004 of the Bank as the Overall Winner, the Winner of the Financial Sector and the Winner of Corporate Governance Disclosure Award. Won three awards at the 'National Business Excellence Awards - 2005' organised by the National Chamber of Commerce. Raises US \$ 65 million 2-year syndicated loan with an option to extend it for a further year at the option of the lender, the first such loan by a non-sovereign corporate in the country. Makes a scrip issue on the basis of 1:1. Introduces the first mobile ATM in the country.

**2006** Rated as the Best Bank in Sri Lanka by "Global Finance" for the 8th consecutive year. Fitch Ratings Lanka Ltd., upholds the AA+ (lka) rating in their annual review. SAFA rated Annual Report 2005 as the Winner in the Best presented Accounts in the Banking Institutions Sector and also as the Winner of the inaugural award for the Corporate Governance Disclosure. The ICASL ranked the Annual Report 2005 of the Bank as the Overall Winner and the Winner of the Banking Sector for the 5th consecutive year. Won 5 main awards including the Overall Winner award at the "National Business Excellence Awards - 2006" organised by the National Chamber of Commerce. Raised US \$ 10 Mn. by issuing five year bonds, the first of its kind by an indigenous bank in Sri Lanka.



Country	Name & Address of the Bank	BIC Code/Swift	CCY	Account No.	Website
Australia	1 Citygroup Pty Ltd. ABN 88 004 325 080, AFSL 238098 G.P.O. Box 40, Sydney NSW 1027 - Australia	CITIAU2X	AUD	205636005 *	citibank.com.au
	2 National Australia Bank 11/120, Spencer Street, Melbourne Victoria 3000 - Australia	NATAAU33033	AUD	1803020052500	national.com.au
Bangladesh	3 Commercial Bank of Ceylon Ltd. 47, Motijheel Commercial Area, P.O. Box 3490, Dhaka 1000, Bangladesh	CCEYBDDH	AC\$	2-802000017	combank.net
Belgium	4 Fortis Bank NV/SA Montagne DU PARC 3, B-1000, Brussels, Belgium	GEBABEBB	EUR	291-1179210-78	fortis.com
Canada	5 Canadian Imperial Bank of Commerce Int'l Dept. Head Office, Commerce Court, Toronto M5L 1H1, Canada	CIBCCATT	CAD	1733117 1751514 *	cibc.com
Denmark	6 Nordea Bank Denmark A/S P.O. Box 850, DK-0900, Copenhagen, Denmark	NDEADKKK	DKK	5000408909 5000017703 *	nordea.com
France	7 Credit Agricole SA, 75710 Paris Cedex 15, CCP, Paris 702 U 020 France	AGRIFRPP	EUR	20533624000 *	credit-agricole.fr
Germany	8 American Express Bank GmbH Data & Exposure Control, P.O. Box 110162 Theodor - Heuss - Allee 112, D60036 Frankfurt AM Main, Germany	AEIBDEFX	EUR	018109406 018112204 *	amexbank.de
	9 Bayerische Hypo und Vereins Bank AG D-80311 Muenchen, Germany	HYVEDEMM	EUR	69101429	hvb.com hvb.de
	10 Commerz Bank AG ZTB BC Mitte 6.4, Mainzer Landstrasse 277-293, 60261, Frankfurt AM Main, Germany	COBADEFF	EUR	400872103701 400871436200 *	commerzbank.com
	11 West LB AG Girozentrale-P.O. Box D40199, Dusseldorf, Germany	WELADED	EUR	59031/EUR	westlb.com westlb.de

\* Accounts of Bangladesh Operation

## Correspondent Banks

Country	Name & Address of the Bank	BIC Code	CCY	Account No.	Website
<b>Hong Kong</b>	<b>12</b> Standard Chartered Bank P.O. Box 21, 9th Floor, 4-4A, Des Voeux Road, Central Hong Kong	SCBLHKHH	HKD	41109468048 44709419107 *	standardchartered.com
<b>India</b>	<b>13</b> American Express Bank Ltd. 187, Mount Road, Chennai 600 006, India	AEIBINXMAS	AC\$	510280024	americanexpress/india.com
	<b>14</b> Calyon Bank, Mumbai, India	BSUIINBB	AC\$	00712402150000USD *	calyon.com
	<b>15</b> ICICI Bank Ltd. ICICI Bank Towers, Bandra-Kurla Complex, Bandra (East), Mumbai 400 051, India	ICICINBB	AC\$	000406000181 000406000220 *	icicibank.com
	<b>16</b> Standard Chartered Bank 23-25, Mahathma Gandhi Road, P.O. Box 558, Mumbai 400 001, India	SCBLINBB	AC\$	22205031885	standardchartered.com
<b>Iran</b>	<b>17</b> Bank Melli Iran Int'l Dept. Asian Section, P.O. Box 11365-171, Ferdowsi Avenue, Tehran, Iran	MELIIRTH	AC\$	12-08-504	bmi.ir
<b>Italy</b>	<b>18</b> Banca Intesa BCI #2612 Head Office, Int'l Money Transfer Dept., Piazza Della Scala 6, 20121 Milan, Italy	BCITITMM	EUR	9629220249	bancaintesa.it
	<b>19</b> Capitalia Societa Per Azioni Viale, Mberto, Tutini, 180, 1-00144 Rome, Italy	BROMITRR	EUR	1000271	capitalia.it
<b>Japan</b>	<b>20</b> Bank of Tokyo Mitsubishi Ltd., P.O. Box 191, Nihonbashi, Tokyo - Japan	BOTKJPJT	JPY	653-0461318 *	bk.mufig.jp
	<b>21</b> Standard Chartered Bank P.O. Box 9997, 21st Floor, Sanno Park, Tower 2-11-1, Nagata-cho, Chiyoda-ku, Tokyo 100-6155, Japan	SCBLJPJT	JPY	2168531110	standardchartered.com
<b>Korea</b>	<b>22</b> Kookmin Bank 9-1, 2GA, Namdaemun - RO, Jung - GU, Seoul 100-703, Korea	CZNBKRSE	US\$	759-8-US\$-01-0 761-8-US\$-01-3 *	kbstar.com
<b>Netherlands</b>	<b>23</b> ABN Amro Bank N.V. 32, Vijzelstraat, P.O. Box 669, Amsterdam, Netherlands	ABNANL2A	EUR	540427349	abnamro.com
	<b>24</b> Ing Bank N.V. P.O. Box 1800 1000 BV., Amsterdam, Netherlands.	INGBNL2A	EUR	0050908928	Ing.com
<b>New Zealand</b>	<b>25</b> Bank of New Zealand P.O. Box 2392, 1, Willis Street, Wellington, New Zealand	BKNZNZ22	NZD	2659680000 2690700000 *	bnz.co.nz
<b>Norway</b>	<b>26</b> Den Norske Bank Stranden 21, 0021, Oslo, Norway	DNBANOKK	NOK	7002-02-04808	dnbnor.com
<b>Pakistan</b>	<b>27</b> Habib Bank AG Zurich P.O. Box 1424, Hirani Centre, 1.1, Chundrigar Road, Karachi 74200, Pakistan	HBZUPKKA	AC\$	20110-333-31503	habibbank.com
	<b>28</b> Standard Chartered Bank 1.1, Chundrigar Road, Karachi 75600, Pakistan	SCBLPKKA	AC\$	15000297601 15000288701 *	standardchartered.com
<b>Saudi Arabia</b>	<b>29</b> The National Commercial Bank International Banking Division, Banking Relations, 20th Floor, P.O. Box 3555, Jeddah 21481, Saudi Arabia	NCBKSJAE	US\$	55535150090301	alahli.com
<b>Singapore</b>	<b>30</b> Standard Chartered Bank P.O. Box 1901, 6, Battery Road, 7th Storey, Singapore 049909	SCBLSGSG	SGD	0109344561	standardchartered.com
	<b>31</b> United Overseas Bank Ltd., 80, Raffles Place 08-01, UOB Plaza 1, Singapore 048624	UOVBSGSG	SGD	1013992113 *	uobgroup.com
<b>Sri Lanka</b>	<b>32</b> Commercial Bank of Ceylon Ltd., Commercial House, 21, Bristol Street, P.O. Box 856, Colombo 1, Sri Lanka	CCEYLK LX	AC\$	1420825031 *	combank.net

\* Accounts of Bangladesh Operation

## Correspondent Banks

Country	Name & Address of the Bank	BIC Code	CCY	Account No.	Website
Sweden	33 Skandinaviska Enskilda Banken Utlandsreskontran Stockholm S 106 40, Sweden	ESSESESS	SEK	52018529803	sebgrou.com
	34 Svenska Handelsbanken Stockholm, Sweden	HANDESSA	SEK	40324079 *	handelsbanken.com
Switzerland	35 UBS A.G. P.O. Box CH-8098, Zurich, Switzerland	UBSWCHZH	CHF	0230-00085408 0230-00036535 *	ubs.com
United Kingdom	36 HSBC Bank PLC, 8, Canada Square, London - UK	MIDLGB22	GBP GBP EUR	58335536 * 59398188 * 59448448 *	hsbc.co.uk
	37 Standard Chartered Bank City Office, Branch No. 37, Grace Church Street, London EC3V OBX, UK	SCBLGB2L	GBP EUR	01804813401 01804813496	standardchartered.com
United States of America	38 American Express Bank 300, Boulevard East, Weehawken, NJ 07086, U.S.A.	AEIBUS33	US\$	000724989	americanexpress.com
	39 Bank of America NT & SA International Deposit Services, 1850 Gateway BL VD, 6th Floor, Concord CA 94520, U.S.A.	BOFAUS6S	US\$	6290890098	bankofamerica.com
	40 Citi Bank 111, Wall Street, 19th Floor, New York 10043, U.S.A.	CITIUS33	US\$	36141446 36241316 *	citibank.com
	41 Deutsche Bank Trust Company Americas P.O. Box 318, Church Street Station, New York, NY 10008, U.S.A.	BKTRUS33	US\$	04034566	db.com
	42 HSBC Bank U.S.A. 500, Stanton Christiana Road, Newark Delaware 19713, NY - U.S.A.	MRMDUS33	US\$	000045829 000147605 *	hsbcusa.com
	43 JP Morgan Chase Bank Head Office, 270, Park Avenue, New York, NY 10017, U.S.A.	CHASUS33	US\$	400808625 400809176 *	jpmorganaccess.com
	44 Standard Chartered Bank One Madison Avenue, New York NY 10010-3603 U.S.A.	SCBLUS33	US\$	3582052360001 3582052637001 *	standardchartered.com
45 Wachovia Bank N.A. 11, Penn Plaza, 4th Floor, New York, NY 10038, USA	PNBPUS3NNYC	US\$	2000191002407 2000193003365 *	wachovia.com	

\* Accounts of Bangladesh Operation

# Network of Delivery Points

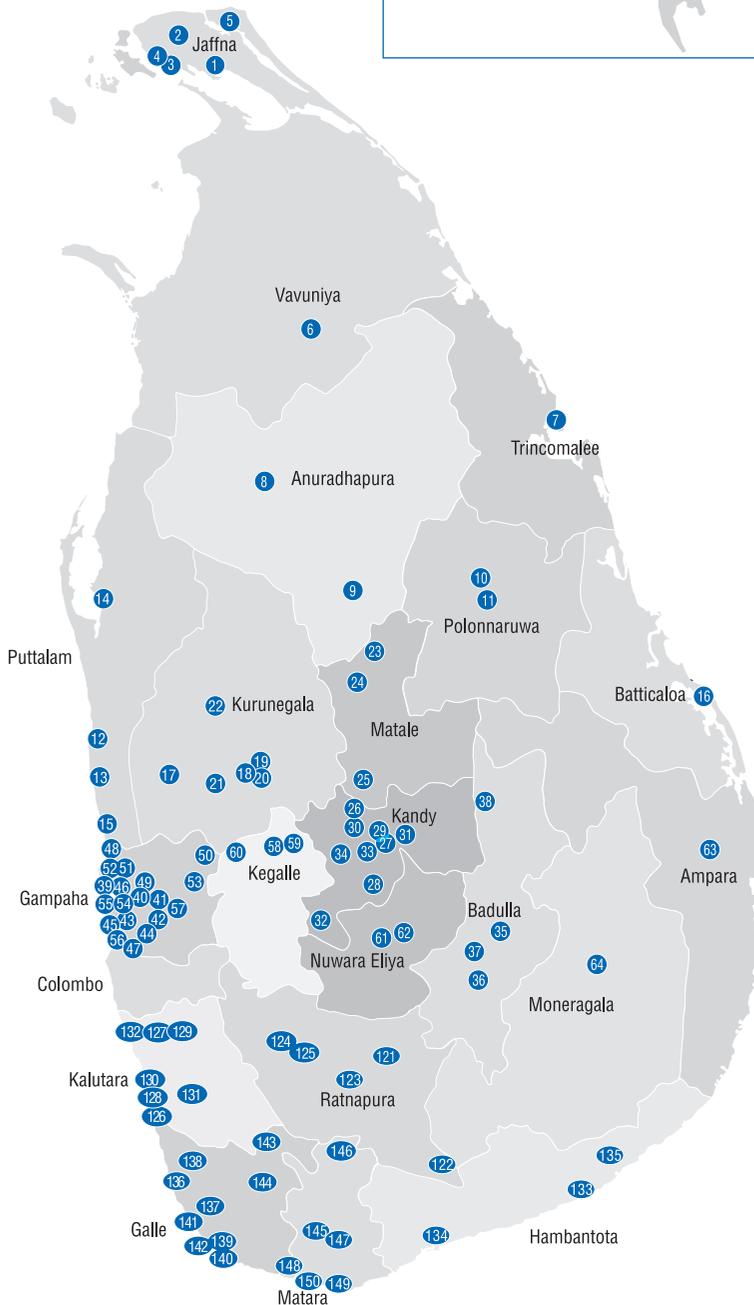
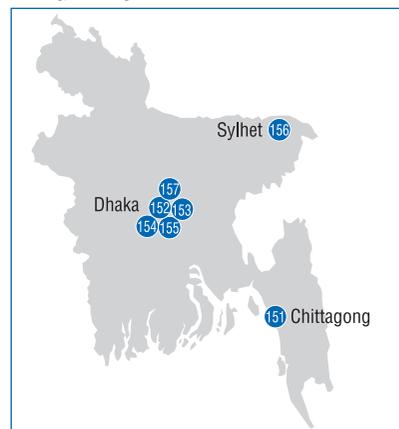
## BRANCHES IN SRI LANKA

<b>Jaffna District</b>		Kiribathgoda	47
Chavakachcheri*	1	Kochchikade	48
Chunnakam	2	Minuwangoda	49
Jaffna	3	Mirigama	50
Jaffna CSP*	4	Negombo	51
Nelliady	5	Negombo 2nd	52
<b>Vavuniya District</b>		Nittambuwa	53
Vavuniya	6	Raddolugama*	54
<b>Trincomalee District</b>		Seeduwa	55
Trincomalee	7	Wattala	56
<b>Anuradhapura District</b>		Yakkala	57
Anuradhapura	8	<b>Kegalle District</b>	
Kekirawa	9	Kegalle	58
<b>Polonnaruwa District</b>		Mawanella	59
Hingurakgoda	10	Warakapola*	60
Kaduruwela	11	<b>Nuwara-Eliya District</b>	
<b>Puttalam District</b>		Hatton	61
Chilaw	12	Nuwara-Eliya	62
Nattandiya	13	<b>Ampara District</b>	
Palavi CSP	14	Ampara	63
Wennappuwa	15	<b>Moneragala District</b>	
<b>Batticaloa District</b>		Moneragala	64
Batticaloa	16	<b>Colombo District</b>	
<b>Kurunegala District</b>		<i>Please refer page 173</i>	
Kuliyapitiya	17	<b>Ratnapura District</b>	
Kurunegala	18	Balangoda	121
Kurunegala CSP	19	Embilipitiya	122
Kurunegala MiniCom	20	Kahawatte*	123
Narammala	21	Ratnapura	124
Nikaweratiya	22	Ratnapura MiniCom	125
<b>Matale District</b>		<b>Kalutara District</b>	
Dambulla	23	Aluthgama	126
Galewela	24	Bandaragama	127
Matale	25	Beruwela MiniCom*	128
<b>Kandy District</b>		Horana	129
Akurana MiniCom*	26	Kalutara	130
Aniwatte SP	27	Matugama	131
Gampola	28	Panadura	132
Kandy	29	<b>Hambantota District</b>	
Katugastota	30	Ambalantota	133
Kundasale SP*	31	Tangalle	134
Nawalapitiya	32	Tissamaharama	135
Peradeniya	33	<b>Galle District</b>	
Piimatalawa	34	Ambalangoda	136
<b>Badulla District</b>		Baddegama	137
Badulla	35	Elpitiya	138
Bandarawela	36	Galle City	139
Welimada*	37	Galle Fort	140
Mahiyanganaya*	38	Hikkaduwa	141
<b>Gampaha District</b>		Karapitiya*	142
Airport Counter	39	Neluwa*	143
Ekala	40	Udugama*	144
Gampaha	41	<b>Matara District</b>	
Gampaha MiniCom	42	Akuressa	145
Ja-Ela	43	Deniyaya	146
Kadawatha	44	Kamburupitiya	147
Kandana	45	Koggala	148
Katunayake FTZ	46	Matara	149
		Weligama	150

## OVERSEAS BRANCHES

<b>Bangladesh</b>	
Chittagong	151
Dhaka	152
Dhanmondi	153
Gulshan Booth	154
Sonargaon Booth	155
Sylhet*	156
Uttara*	157

## BANGLADESH



\*Opened in 2006

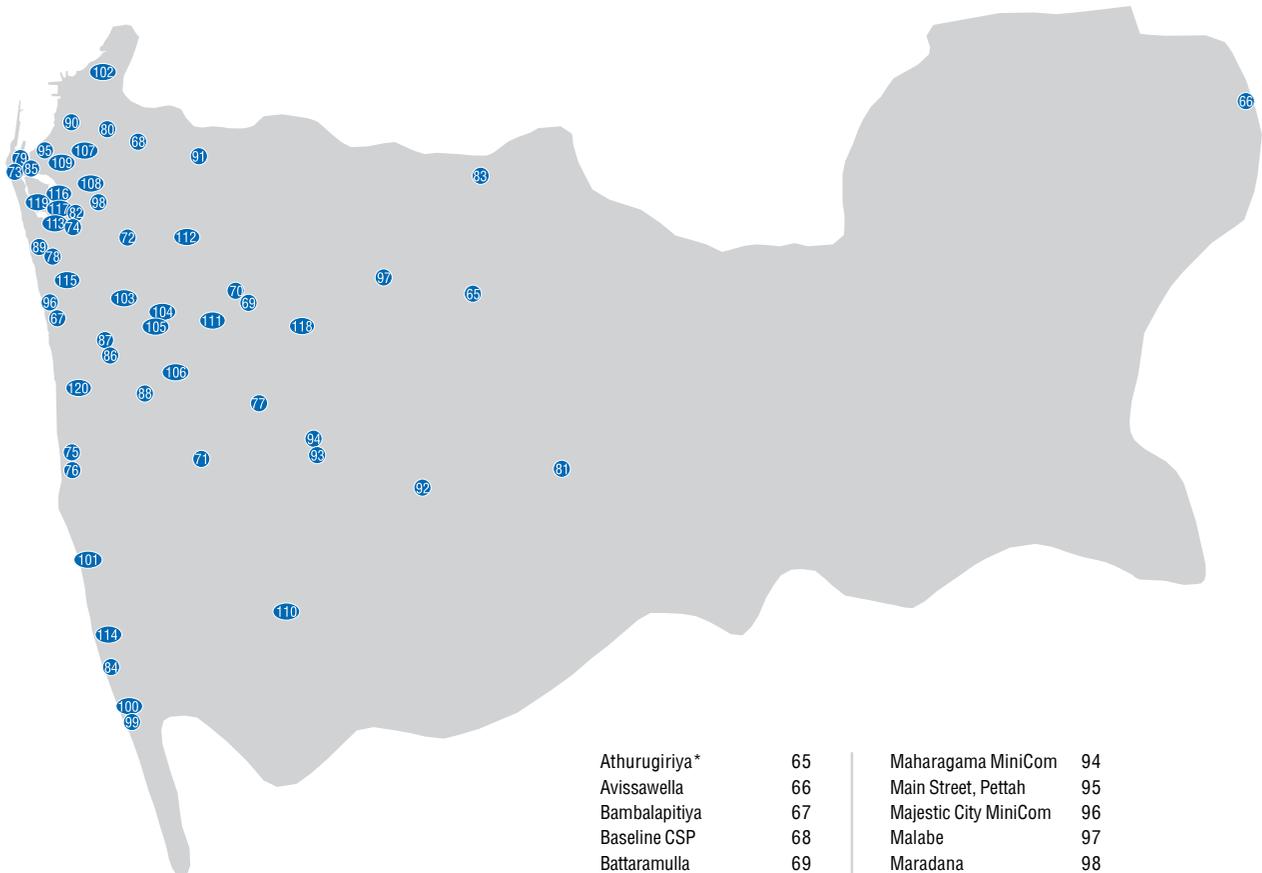
ASP - Banking Centres at Arpico Supercentres

CSP - Customer Service Point

MiniCom - Banking Centres at Cargills Food City Supermarkets

SP - Service Point

COLOMBO DISTRICT



Athurugiriya*	65	Maharagama MiniCom	94
Avissawella	66	Main Street, Pettah	95
Bambalapitiya	67	Majestic City MiniCom	96
Baseline CSP	68	Malabe	97
Battaramulla	69	Maradana	98
Battaramulla ASP	70	Moratuwa	99
Boralesgamuwa SP*	71	Moratuwa MiniCom	100
Borella	72	Mt. Lavinia	101
City Office	73	Mutwal	102
Colombo 7 (Town Hall)	74	Narahenpita	103
Dehiwala	75	Nawala	104
Dehiwala ASP	76	Nawala MiniCom	105
Delkanda CSP*	77	Nugegoda	106
Duplication Road	78	Old Moor Street	107
Foreign Branch/ Head Office	79	Panchikawatte	108
Grandpass	80	People's Park, Pettah	109
Homagama	81	Piliyandala	110
Hyde Park Corner ASP	82	Pita Kotte CSP	111
Kaduwela	83	Rajagiriya	112
Katubedda CSP	84	Ramanayake Mw CSP	113
Keyzer Street	85	Ratmalana	114
Kirulapone	86	Reid Avenue/Priority Banking Centre	115
Kirulapone MiniCom	87	Sri Lanka Insurance Corp. CSP	116
Kohuwala	88	Staples Street MiniCom	117
Kollupitiya	89	Thalawathugoda	118
Kotahena	90	Union Place	119
Kotahena Savings Centre		Wellawatte	120
Kotikawatte	91		
Kottawa	92		
Maharagama	93		

\*Opened in 2006  
 ASP - Banking Centres at Arpico Supercentres  
 CSP - Customer Service Point  
 MiniCom - Banking Centres at Cargills Food City Supermarkets  
 SP - Service Point

## Snapshot of the Sri Lankan Economy

As at February 15, 2007

GDP - 2005	Rs.Bn.	US \$ Bn.	External Sector	US \$ Mn.	2006	Change %		
At Current Market Prices	2,366	23.19	Textile & Apparel Exports		3,080.4	6.4		
GDP Growth Rate	%	2006	2005	Tea Exports	881.2	8.8		
03rd Quarter	7.5	6.9	Exports		6,882.7	8.4		
First 09 months	7.8	5.8	Imports		10,253.0	15.7		
Full Year	7.0 <sup>e</sup>	6.0	Private Remittances - Net		2,075.4	23.1		
Exchange Rate - Rs./US\$ (End - Year)	107.50	102.02						
					2006	2005		
Rate of Inflation	%	2007	Y.A.	Balance of Payment (BoP)	193	501		
CCPI Annual Avg. Change	Jan.	14.8	11.1		2006	Change %		
CCPI Point-to-Point Change	Jan.	20.5	8.0		End Dec.	From Dec. '05		
SLCPI Annual Avg. Change	Dec. 06	9.5	10.6	Gross Official Reserves	2,515.2	2.3		
Interest Rates	%	15.02.07	Y.A.	Change in Money Supply %	Dec 06	M.A.	Y.A.	
AWPLR		15.01	12.04	M <sub>2</sub> b (YoY)	17.8	16.9	19.1	
SLIBOR - 01 day		13.17	10.28	Government Finance	Rs. Bn.	2006 <sup>e</sup>	2005	06 Budget
Call Money Rate (Weekly Average)		13.05	10.06	Govt. Revenue		482.2	379.7	484.4
Treasury Bills - 03 months		13.75	10.11	Govt. Expenditure		721.9	584.8	731.6
Treasury Bills - 12 months		14.09	10.37	Budget Deficit as % of GDP		8.7	8.7	9.1
Treasury Bonds - 02-year		13.32	10.69	Government Debt	Rs. Bn.	2006	2005	Share (%)
Treasury Bonds - 03-year		13.10	11.16			End Nov.	End Nov.	2006
		Jan. 2007	Y.A.	Domestic Debt		1,455.1	1,257.1	57.3
AWDR		7.60	6.34	Foreign Debt		1,082.4	926.8	42.7
AWFDR		11.56	9.18	Total Debt		2,537.5	2,183.8	100.0
		15.02.07	Y.A.	Total Debt as % of GDP (2005)		N/A	92.3	
Repo		10.00	8.75	Share Market	As at Feb. 14	2006	2005	
Reverse Repo		11.50	10.25	All Share Price Index (ASPI)		3,011	2,161	
Tourism		2006	Change %	Milanka Price Index (MPI)		4,182	2,735	
Tourist Arrivals ('000)		559.6	1.9	Avg. Daily Turnover (Rs. Mn.)		1,139	285	
Earnings from Tourism (US\$ Mn.)		440.9	33.9	Market Capitalisation (Rs. Bn.)		937.1	656.7	

e - Estimate M.A. - Month Ago Y.A. - Year Ago N/A - Not Available/Applicable

- AWPLR - Average Weighted Prime Lending Rate of commercial banks
- SLIBOR - Sri Lanka Inter-Bank Offer Rate
- AWDR - Average Weighted Deposit Rate of commercial banks
- AWFDR - Average Weighted Fixed Deposit Rate of commercial banks
- Repo - Central Bank Overnight Repurchase Rate
- Reverse Repo - Central Bank Overnight Reverse Repurchase Rate

Source: Central Bank of Sri Lanka

### Acceptances

Promise to pay created when the drawee of a time draft stamps or writes the words "accepted" above his signature and a designated payment date.

### Accrual Basis

Recognising the effects of transactions and other events when they occur without waiting for receipt or payment of cash or its equivalent.

### Associate

An entity, including an unincorporated entity such as a partnership, over which the investor has significant influence and that is neither a subsidiary nor an interest in a joint venture.

### Bills for Collection

A bill of exchange drawn by an exporter usually at a term, on an importer overseas and brought by the exporter to his bank with a request to collect the proceeds.

### Bonus Issue (Scrip Issue)

The issue of new shares to existing shareholders in proportion to their shareholdings. It is a process for converting a company's reserves (in whole or part) into issued capital and hence does not involve an infusion of cash.

### Capital Adequacy Ratios

The relationship between capital and risk weighted assets as defined in the framework developed by the Bank for International Settlements and as modified by the Central Bank of Sri Lanka to suit local requirements.

### Cash Equivalents

Short term highly liquid investments that are readily convertible to known amounts of cash and which are subject to an insignificant risk of changes in value.

### Commitments

Credit facilities approved but not yet utilised by the clients as at the Balance Sheet date.

### Compounded Annual Growth Rate

The rate at which it would have grown if it grew at an even rate compounded annually.

### Contingencies

A condition or situation existing at Balance Sheet date where the outcome will be confirmed only by occurrence or non-occurrence of one or more future events.

### Cost /Income Ratio

Operating expenses excluding Loan Loss Provision as a percentage of income.

### Cost Method

A method of accounting whereby the investment is recorded at cost. The Income Statement reflects income from the investment only to the extent that the investor receives distributions from accumulated net profits of the investee arising subsequent to the date of acquisition.

### Corporate Governance

The process by which corporate entities are governed. It is concerned with the way in which power is exercised over the management and direction of entity, the supervision of executive actions and accountability to owners and others.

### Dealing Securities

Marketable securities that are acquired and held with the intention of reselling them in the short-term.

### Deferred Taxation

Sum set aside for tax in the Financial Statements that may become payable in a financial year other than the current financial year.

### Dividend Cover

Profit after tax divided by gross dividends. This ratio measures the number of times dividend is covered by current year's distributable profits.

### Documentary Credits

Commercial letters of credit provided for payment by a bank to the named beneficiary usually the seller of merchandise, against delivery of documents specified in the credit.

### Earnings per Ordinary Share (EPS)

Profit attributable to ordinary shareholders divided by the number of ordinary shares in issue.

### Economic Value Added

A measure of productivity which takes into consideration cost of total invested equity.

### Effective Tax Rate

Provision for taxation excluding deferred tax divided by the profit before taxation.

### Equity Method

A method of accounting whereby the investment is initially recorded at cost and adjusted thereafter for the post acquisition change in the investor's share of net assets of the investee. The Income Statement reflects the investor's share of the results of operations of the investee.

### Finance Lease

A contract whereby a lessor conveys to the lessee the right to use an asset for rent over an agreed period of time which is sufficient to amortise the capital outlay of the lessor. The lessor retains ownership of the asset but transfers substantially all the risks and rewards of ownership to the lessee.

### Foreign Exchange Profit

Profit earned on foreign currency transactions arising from the difference in foreign exchange rates between the transaction/last Balance Sheet date and the settlement/Balance Sheet date. Also arises from trading in foreign currencies.

### Foreclosed Properties

Properties acquired in full or partial satisfaction of debts.

### Forward Exchange Contract

Agreement between two parties to exchange one currency for another at a future date at a rate agreed upon today.

### Free Capital

Excess of equity capital over net book value of Property, Plant & Equipment, intangible assets and Investments.

### Gross Dividends

The portion of profits distributed to the shareholders including the tax withheld.

### Guarantees

Three party agreement involving a promise by one party (the guarantor) to fulfil the obligations of a person owning a debt if that person fails to perform.

### Historical Cost Convention

Recording transactions at the actual value received or paid.

### Human Resource Accounting

The Human Resource is considered as an asset (although not brought into the Balance Sheet) and the value is computed to focus attention on the management of this valuable asset.

### Interest in Suspense

Interest suspended on non-performing loans and advances.

### Interest Margin

Net interest income expressed as a percentage of interest earning assets.

## Glossary of Financial & Banking Terms

### Investment Securities

Securities acquired and held for yield or capital growth purposes and are usually held to maturity.

### Interest Spread

Represents the difference between the average interest rate earned and the average interest rate paid on interest earning assets and interest bearing liabilities, respectively.

### Liquid Assets

Assets that are held in cash or in a form that can be converted to cash readily, such as deposits with other banks, bills of exchange, treasury bills.

### Loan Losses and Provisions

Amounts set aside against possible losses on loans, advances and other credit facilities as a result of such facilities becoming partly or wholly uncollectible.

### Market Capitalisation

Number of ordinary shares in issue multiplied by the market value of a share as at the year end.

### Materiality

The relative significance of a transaction or an event the omission or misstatement of which could influence the economic decisions of users of financial statements.

### Net Assets Value per Ordinary Share

Shareholders' funds excluding Preference Shares if any, divided by the number of ordinary shares in issue.

### Net Interest Income

The difference between what a bank earns on assets such as loans and securities and what it pays on liabilities such as deposits, refinance funds and inter-bank borrowings.

### Non-Performing Loans

A loan placed on cash basis (i.e. Interest income is only recognised when cash is received) because, in the opinion of management, there is reasonable doubt regarding the collectibility of principal or interest. Loans are automatically placed on cash basis when a payment is 3 months past due. All loans are classified as non-performing when a payment is 3 months in arrears.

### Off-Balance Sheet Transactions

Transactions that are not recognised as assets or liabilities in the Balance Sheet but which give rise to contingencies and commitments.

### Open Credit Exposure Ratio

Total net non-performing loans expressed as a percentage of regulatory capital base.

### Price Earnings Ratio (P/E Ratio)

Market price of a share divided by earnings per share.

### Provision Cover

Total provisions for loan losses expressed as a percentage of net non-performing loans before discounting for provisions on non-performing loans.

### Prudence

Inclusion of a degree of caution in the exercise of judgement needed in making the estimates required under conditions of uncertainty, such that assets or income are not overstated and liabilities or expenses are not understated.

### Related Parties

Parties where one party has the ability to control the other party or exercise significant influence over the other party in making financial and operating decisions.

### Return on Average Assets (ROA)

Profit after tax divided by the average assets.

### Risk Weighted Assets

On Balance Sheet assets and the credit equivalent of off Balance Sheet assets multiplied by the relevant risk weighting factors.

### Repurchase Agreement

Contract to sell and subsequently repurchase securities at a specified date and price.

### Reverse Repurchase Agreement

Transaction involving the purchase of securities by a bank or dealer and resale back to the seller at a future date and specified price.

### Return on Average Equity (ROE)

Net profit for the year, less preference share dividends if any, expressed as a percentage of average ordinary shareholders' equity.

### Revenue Reserves

Reserves set aside for future distribution and investment.

### Segmental Analysis

Analysis of financial information by segments of an enterprise specifically, the different industries and the different geographical areas in which it operates.

### Shareholders' Funds

Total of issued and fully paid share capital and capital and revenue reserves.

### Single Borrower Limit

30% of the shareholders' funds (excluding final dividend payable).

### Statutory Reserve Fund

A capital reserve created as per the provisions of the Banking Act No. 30 of 1988.

### Substance Over Form

The consideration that the accounting treatment and the presenting in financial statements of transactions and the events should be governed by their substance and financial reality and not merely by legal form.

### Subsidiary

An entity, including an unincorporated entity such as a partnership, that is controlled by another entity (known as the parent).

### Tier I Capital

Core capital representing permanent shareholders' equity and reserves created or increased by appropriations of retained earnings or other surpluses.

### Tier II Capital

Supplementary capital representing revaluation reserves, general provisions and other capital instruments which combine certain characteristics of equity and debt such as hybrid capital instruments and subordinated term debts.

### Triple Bottom Line Reporting

Reporting on the efforts of a corporate to enhance Shareholder value while being ethical and accountable to the society and environment.

### Unit Trust

An undertaking formed to invest in securities under the terms of a trust deed.

### Value Added

Value of wealth created by providing banking and other related services less the cost of providing such services.

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## Notice of Meeting

Notice is hereby given that the **Thirty-Eighth Annual General Meeting** of Commercial Bank of Ceylon Limited will be held at the 9th Floor of the Union Place Branch of the Bank, No. 1, Union Place, Colombo 2 on Wednesday, March 28, 2007 at 10.30 a.m. for the following purposes:

1. To receive, consider and adopt the Report of the Directors and the Financial Statements for the year ended December 31, 2006 with the Report of the Auditors thereon.
2. To declare a dividend as recommended by the Directors.
3. To re-elect Directors in place of those retiring by rotation or otherwise (\*).
4. To re-appoint Messrs. Ernst & Young as Auditors to the Company for the ensuing year and authorise the Board of Directors to determine their remuneration.
5. To authorise the Board of Directors to determine donations for 2007.

By Order of the Board,

  
**Mrs. R.R. Dunuwille**  
Company Secretary

February 15, 2007  
Colombo

### Notes

1. A member entitled to attend/vote at the Meeting is entitled to appoint a Proxy to attend/vote in his/her stead and a Proxy Holder need not be a member of the Company.
2. A Form of Proxy is sent along with this Report. The completed Form of Proxy should be deposited at the Registered Office of the Company, "Commercial House", No. 21, Bristol Street, Colombo 1, not less than 48 hours before the time appointed for the holding of the Meeting.
3. It is proposed to post the Dividend Warrants on April 9, 2007, upon approval by the shareholders at the Annual General Meeting.

### (\* ) SPECIAL NOTICE

A special notice has been received by the Company from Union Investments Ltd., a Shareholder of the Bank informing their intention to move the following resolution:

#### **Re-Election of Dr. H. S. Wanasinghe**

We, Union Investments Ltd., a shareholder of the Company hereby give Special Notice of our intention to move the following resolution, as an ordinary resolution, at the forthcoming Annual General Meeting of the Company.

"That the age limit stipulated in Section 181 of the Companies Act No. 17 of 1982 shall not be applicable to Dr. Henry Shelton Wanasinghe who attained the age of 80 years on June 16, 2006 and that he be re-elected a Director of the Company."





## Form of Proxy (Voting Shareholders)

I/We .....  
of .....  
being a member/s of Commercial Bank of Ceylon Ltd. hereby appoint .....  
of ..... whom failing:

Mr. Mahendra Jayanthipal Chandima Amarasuriya	whom failing
Mr. Bentotage Robert Lakshman Fernando	whom failing
Mr. Amitha Lal Gooneratne	whom failing
Dr. Henry Shelton Wanasinghe	whom failing
Mr. Anthony Nihal Fonseka	whom failing
Mr. Lalin Joseph Ainsley Fernando	whom failing
Mr. Dinesh Stephen Weerakkody	whom failing
Deshamanya Kandiah Balendra	

as my/our Proxyholder to represent me/us and\* .....  
to vote for me/us on my/our behalf as indicated below at the Thirty-Eighth Annual General Meeting of the Company to be held on March 28, 2007 and at any adjournment thereof and at every poll which may be taken in consequence thereof.

	For	Against
1. To receive, consider and adopt the Report of the Directors and the Financial Statements for the year ended December 31, 2006 with the Report of the Auditors thereon.	<input type="checkbox"/>	<input type="checkbox"/>
2. To declare a Dividend as recommended by the Directors.	<input type="checkbox"/>	<input type="checkbox"/>
3. To re-elect Directors in place of those retiring by rotation:		
(a) Mr. B.R.L. Fernando	<input type="checkbox"/>	<input type="checkbox"/>
(b) Dr. H.S. Wanasinghe	<input type="checkbox"/>	<input type="checkbox"/>
(c) Deshamanya Kandiah Balendra	<input type="checkbox"/>	<input type="checkbox"/>
4. (a) To reappoint Messrs Ernst & Young, as recommended by the Board of Directors as Auditors of the Company	<input type="checkbox"/>	<input type="checkbox"/>
(b) To authorise the Board of Directors to determine the remuneration of the Auditors	<input type="checkbox"/>	<input type="checkbox"/>
5. To authorise the Board of Directors to determine donations for 2007.	<input type="checkbox"/>	<input type="checkbox"/>

In witness my/our hand/seal given on this ..... day of March, Two Thousand and Seven.

.....  
Signature/s

(Please indicate with an 'X')

\* If you wish your Proxyholder to speak at the meeting you should insert the words "to speak and" in the space indicated with the asterisk and initial such insertion.

## Form of Proxy (Voting Shareholders)

- Notes**
- i. Instructions as to completion of this Form of Proxy are given below.*
  - ii. As regards voting on the Resolutions indicated in the Form of Proxy if no words are struck out or there is in the view of the Proxyholder doubt (by reason of the way in which the instructions in the Form of Proxy have been stated by the Shareholder) as to the way in which the Proxyholder should vote, the Proxyholder will vote as he thinks fit.*
  - iii. If the Form of Proxy is signed by an Attorney, the relative Power of Attorney (POA) should accompany the completed Form of Proxy for registration, if such POA has not already been registered with the Company.*
  - iv. If the Shareholder is a company or a corporate body, the Form of Proxy should be executed under its common seal or signed by its Attorney or by an officer on behalf of the Company/corporate body, in accordance with its Articles of Association/Statute.*

### Instructions as to Completion of Form of Proxy

- (i) Article 67 of the Articles of Association of the Company provides that:

“ The instruments appointing a Proxy shall be in writing, and

- (a) in the case of an individual shall be signed by the Appointer or by his Attorney; and
- (b) in the case of a corporation shall be either under its common seal or signed by its Attorney or by an Officer on behalf of the corporation.

The Company may, but shall not be bound to, require evidence of the Authority of any such Attorney or Officer. A Proxy need not be a member of the Company.”

- (ii) The full name(s) and address(es) of the Proxyholder and of the Shareholder appointing the Proxyholder should be entered legibly in the Form of Proxy.
- (iii) The completed Form of Proxy should be deposited with the Company Secretary at the Registered Office of the Company, No. 21, Bristol Street, Colombo 1, not less than 48 hours before the time fixed for the holding of the meeting.

**Form of Proxy (Non-Voting Shareholders)**

I/We .....  
of .....  
being a member/s of Commercial Bank of Ceylon Ltd. hereby appoint .....  
of ..... whom failing:

Mr. Mahendra Jayanthipal Chandima Amarasuriya	whom failing
Mr. Bentotage Robert Lakshman Fernando	whom failing
Mr. Amitha Lal Gooneratne	whom failing
Dr. Henry Shelton Wanasinghe	whom failing
Mr. Anthony Nihal Fonseka	whom failing
Mr. Lalin Joseph Ainsley Fernando	whom failing
Mr. Dinesh Stephen Weerakkody	whom failing
Deshamanya Kandiah Balendra	

as my/our Proxyholder to represent me/us and\* .....  
at the Thirty-Eighth Annual General Meeting of the Company which is scheduled to be held on March 28, 2007 and at any adjournment thereof.

In witness my/our hand/seal given on this ..... day of March, Two Thousand and Seven.

.....  
Signature/s

\* If you wish your Proxyholder to speak at the meeting you should insert the words "to speak and" in the space indicated with the asterisk and initial such insertion.

## Form of Proxy (Non-Voting Shareholders)

- Notes**
- i. Instructions as to completion of this Form of Proxy are given below.*
  - ii. Shareholders of non-voting shares are entitled only to attend and speak at the meeting.*
  - iii. If the Form of Proxy is signed by an Attorney, the relative Power of Attorney (POA) should accompany the completed Form of Proxy for registration, if such POA has not already been registered with the Company.*
  - iv. If the Shareholder is a company or a corporate body, the Form of Proxy should be executed under its common seal or signed by its Attorney or by an officer on behalf of the Company/corporate body in accordance with its Articles of Association/Statute.*

### Instructions as to Completion of Form of Proxy

- (i) Article 67 of the Articles of Association of the Company provides that:

“ The instruments appointing a Proxy shall be in writing, and

- (a) in the case of an individual shall be signed by the Appointer or by his Attorney; and
- (b) in the case of a corporation shall be either under its common seal or signed by its Attorney or by an Officer on behalf of the corporation.

The Company may, but shall not be bound to, require evidence of the authority of any such Attorney or Officer. A Proxy need not be a member of the Company.”

- (ii) The full name(s) and address(es) of the Proxyholder and of the Shareholder appointing the Proxyholder should be entered legibly in the Form of Proxy.
- (iii) The completed Form of Proxy should be deposited with the Company Secretary at the Registered Office of the Company, No. 21, Bristol Street, Colombo 1, not less than 48 hours before the time fixed for the holding of the meeting.

**Name of Company**

Commercial Bank of Ceylon Ltd.

**Legal Form**

A public limited liability company incorporated in Sri Lanka on June 25, 1969 under the Companies Ordinance No. 51 of 1938 and quoted in the Colombo Stock Exchange in March 1970. A licensed commercial bank under the Banking Act No. 30 of 1988.

**Company Registration Number**

PBS 600

**Tax Payer Identification Number (TIN)**

124006007

**Stock Exchange Listing**

The Ordinary Shares, 11.25% Cumulative Redeemable Preference Shares and the Unsecured Subordinated Redeemable Debentures of 2003/2008 series, December 2006/December 2011 series, December 2006/December 2013 series and December 2006/December 2016 series, both fixed and floating interest rates of the Company are listed on the Colombo Stock Exchange.

**Registered Office**

"Commercial House",  
No. 21, Bristol Street, P.O. Box 856,  
Colombo 1, Sri Lanka.

Telephone : 2445010-15 (6 lines), 2328193-5 (3 lines)  
2430420, 2336700

Telegraphic Address : COMBANK

Telex : 21520 COMEX CE; 21274 COMBANK CE;

21898 COMFEX CE; 22384 COMFX CE;

23375 COMTLX CE.

Facsimile : 941-2449889

SWIFT Code - Sri Lanka : CCEYLKX

SWIFT Code - Bangladesh : CCEYBDDH

E-mail : email@combank.net

Website : www.combank.net

**Head Office**

"Commercial House", No. 21, Bristol Street,  
P.O. Box 856, Colombo 1, Sri Lanka.

*For any clarifications on this Report please write to:*

**The Company Secretary,  
Commercial Bank of Ceylon Ltd.,  
"Commercial House",  
No. 21, Bristol Street,  
Colombo 1, Sri Lanka.**

**or e-mail to: email@combank.net**

*Minimise waste by informing the Commercial Bank Company Secretary to update the mailing list if you are receiving more than one copy of the Annual Report.*

**Board of Directors**

Mr. M.J.C. Amarasuriya (*Chairman*)  
Mr. B.R.L. Fernando (*Deputy Chairman*)  
Mr. A.L. Gooneratne (*Managing Director*)  
Dr. H.S. Wanasinghe  
Mr. A.N. Fonseka  
Mr. L.J.A. Fernando  
Mr. Iyad M. Malas  
Mr. D.S. Weerakkody  
Mr. G. Galludec (*Alternate Director*)  
Deshamanya Ken Balendra

**Company Secretary**

Mrs. R.R. Dunuwille

**Audit Committee**

Mr. B.R.L. Fernando (*Chairman*)  
Mr. A.L. Gooneratne (by invitation)  
Dr. H.S. Wanasinghe  
Mr. A.N. Fonseka

**Compliance Officer**

Mr. Delip Fernando - Deputy General Manager (Inspection)

**Auditors**

Ernst & Young,  
Chartered Accountants,  
No. 201, De Saram Place,  
P.O. Box 101,  
Colombo 10, Sri Lanka.

**Lawyers**

Julius & Creasy,  
No. 41, Janadhipathi Mawatha,  
Colombo 1, Sri Lanka.

**Credit Rating**

The Bank received AA+(Ika) credit rating from Fitch Ratings Lanka Ltd.  
The Bank's Bangladesh Operations received AA credit rating from Credit Rating Information Services Ltd.

**Corporate Responsibility Rating**

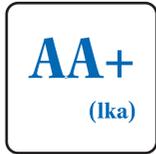
The Bank received B+ Corporate Responsibility Rating from Det Norske Veritas (DNV).

**Subsidiary Companies**

<b>Name of the Company</b>	<b>Holding</b>	<b>Principal Activity</b>
Commercial Bank Primary Dealer Ltd.	100.00%	Primary Dealer for Government Securities
ONEzero Company Ltd.	100.00%	Provision of IT related Services
X-pertise Ltd.	100.00%	Training and Development of Human Resource
Commercial Development Company Ltd.	94.55%	Property Development

**Associate Companies**

<b>Name of the Company</b>	<b>Holding</b>	<b>Principal Activity</b>
Commercial Fund Management (Pvt.) Ltd. (Disposed on January 23, 2007)	50.00%	Fund Management
Commercial Leasing Company Ltd.	30.00%	Leasing, Factoring, Hire Purchase and Hiring of Vehicles
Equity Investments Lanka Ltd.	22.92%	Venture Capital



*From Fitch  
Ratings Lanka Ltd.*



*From Credit Rating  
Information Services Ltd.  
for Bangladesh Operations*



*From Det Norske  
Veritas for  
Corporate Responsibility*

Commercial Bank is widely hailed as the No.1 Private Bank in Sri Lanka. As of end December 2006, Assets, Loans & Advances and Deposits stood at Rs. 224 Billion, Rs.156 Billion and Rs. 157 Billion respectively.

Commercial Bank also has an extensive on-line real time network of delivery points in Sri Lanka consisting of 150 branches/service points and the single largest network of 269 ATMs.



COMMERCIAL BANK