Central Bank of Sri Lanka - 2021

1.1 Opinion

The audit of the financial statements of Central Bank of Sri Lanka (the "Bank"), which comprise the statement of financial position as at 31 December 2021, and the statement of income, statement of other comprehensive income, statement of changes in equity and statement of cash flows for the year then ended, and notes to the financial statements, including a summary of significant accounting policies, was carried out under my direction in pursuance of provisions in Article 154(1) of the Constitution of the Democratic Socialist Republic of Sri Lanka read in conjunction with provisions of the National Audit Act No. 19 of 2018, Section 13(1) of the Finance Act, No. 38 of 1971 and Section 42(2) of the Monetary Law Act (Chapter 422). My comments and observations which I consider should be report to Parliament appear in this report. To carry out this audit, I was assisted by a firm of Chartered Accountants in public practice to examine the compliance with International Financial Reporting Standards.

In my opinion, the accompanying financial statements give a true and fair view of the financial position of the Bank as at 31 December 2021, and its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards (IFRSs).

1.2 Basis for Opinion

I conducted my audit in accordance with International Standards on Auditing (ISAs). My responsibilities under those standards are further described in the Auditor's Responsibilities for the Audit of the Financial Statements section of my report. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my opinion.

1.3 Responsibilities of Monetary Board and Those Charged with Governance for the Financial Statements

Monetary Board is responsible for the preparation and fair presentation of the financial statements in accordance with IFRSs, and for such internal control as Monetary Board determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, Monetary Board is responsible for assessing the Bank's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless management either intends to liquidate the Bank or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the Bank's financial reporting process.

As per Section 16(1) of the National Audit Act No. 19 of 2018, the Bank is required to maintain proper books and records of all its income, expenditure, assets and liabilities, to enable annual and periodic financial statements to be prepared of the Bank.

1.4 Auditor’s Responsibilities for the Audit of the Financial Statements

My objective is to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes my opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

As part of an audit in accordance with ISAs, I exercise professional judgment and maintain professional skepticism throughout the audit. I also:

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for my opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Bank’s internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by Monetary Board.
- Conclude on the appropriateness of Monetary Board’s use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Bank’s ability to continue as a going concern. If I conclude that a material uncertainty exists, I am required to draw attention in my auditor's report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify my opinion. My conclusions are based on the audit evidence obtained up to the date of my auditor's report. However, future events or conditions may cause the Bank to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

The scope of the audit also extended to examine as far as possible and as far as necessary the following;

- Whether the organization, systems, procedures, books, records and other documents have been properly and adequately designed from the point of view of the presentation of information to enable a continuous evaluation of the activities of the Bank, and whether such systems, procedures, books, records and other documents are in effective operation;
- Whether the Bank has complied with applicable written law, or other general or special directions issued by the governing body of the Bank;
- Whether the Bank has performed according to its powers, functions and duties; and
- Whether the resources of the Bank had been procured and utilized economically, efficiently and effectively within the time frames and in compliance with the applicable laws.

2. Financial Review

2.1 Financial Results

According to the financial statements presented, the operations of the Bank for the year under review had resulted in a net profit of Rs.158.2 billion as compared with the net profit of Rs. 63.4 billion in the preceding year, thus indicating an increase of Rs. 94.8 billion in the financial results. Increase of foreign currency investment income and net income from local currency financial assets were the main reasons attributed for this improvement.

2.2 Trend Analysis of major Income and Expenditure items

Analysis of major income items and major expenditure items of the Bank during the year under review, as compared with the preceding year are shown below.

	2021	2020	Variance [Favorable/(Adverse)]	
	Rs. Bn.	Rs. Bn.	Rs. Bn.	percentage
Income from Foreign Currency Financial Assets	**68.5**	**56.3**	**12.2**	**21.6**
Interest Income	11.8	26.2	(14.4)	(54.9)
Gain/(Loss) from Unrealized Price Revaluations	41.8	23.5	18.3	77.8
Gain/(Loss) from Realized Price Changes	14.8	6.5	8.3	127.6
Expenses on Foreign Currency Financial Liabilities	**3.3**	**7.3**	**4.0**	**54.7**
Interest Expense	5.6	5.3	(0.3)	(5.6)
Expected Credit Losses	2.2	(2.0)	4.2	210.0
Net Foreign Exchange Revaluation Gain/ (Loss)	**34.0**	**7.1**	**26.9**	**378.8**
Total Net Income/(Expense) from Local Currency Financial Assets	**58.9**	**16.9**	**42.0**	**248.5**
Other Income	**16.2**	**1.6**	**14.6**	**912.5**
Operating Expenses	**16.3**	**11.2**	**(5.1)**	**(45.5)**
Tax	**-**	**-**	**-**	**-**
Profit/(Loss) for the year	**158.2**	**63.4**	**94.8**	**149.5**

(a) As per Section 41 of the Monetary Law Act, foreign exchange revaluation gain or loss shall not be included in the computation of the annual profits and losses of the Bank. Therefore, the profit for the year under review was Rs.124.2 billion (excluding net foreign exchange revaluation gain of Rs. 34.0 billion) as compared with the gain of of Rs. 56.3 billion (excluding net foreign exchange revaluation loss of Rs. 7.1 billion) in the preceding year, thus indicating an improvement of Rs.67.9 billion in the profit.

(b) The distributable profit for the year under review as determined in terms of Sections 38 and 41 of the Monetary Law Act and profit distribution policy of the Bank approved by the Monetary Board (effective from 2018) was Rs.74.6 billion as compared with the distributable profit of Rs. 18.6 billion in the preceding year. Accordingly, a sum of Rs.30 billion or 40 per cent had been distributed to the Consolidated Fund out of the distributable profit, after making transfers to reserves out of distributable profit for the year under review as compared with Rs. 15 billion distributed to the Consolidated Fund in the preceding year.

2.3 Trend Analysis of Balance Sheet items of the Bank

(a) According to the annual financial statements of the Bank, the Bank's holding of treasury bills rose to Rs. 1,351 billion (Book value) at the end of year 2021 from Rs.638 billion (Book value) stood at end 2020. It was Rs.43 billion (Book value) and Rs.25 billion (Book value) at the end of years 2018 and 2019 respectively. Accordingly, The Bank's holding of treasury bills raised to around 59.5 per cent of outstanding treasury bills issued by the government at the end of year 2021 from 40.4 per cent at the end of year 2020. It stood at 2.9 per cent end of year 2019.

(b) Secretary to the Treasury had made a request by a letter dated 22 July 2021 from the Bank to issue treasury bill to the Central Bank to meet the Sri Lankan rupee requirement to purchase USD in order to settle international sovereign bond of USD 1,000 million maturing due on 26 July 2021. Further request was made by the Secretary to the Treasury on 30 July 2021 to issue treasury bills worth of Rs. 60 billion to the Central Bank. The Bank informed the Secretary to the Treasury that this request was decided to be accommodated in national interest under exceptional circumstances.

(c) The total value of local currency financial assets had increased substantially to Rs. 2,221.7 billion or 120.7 per cent at the end of year 2021 from Rs.1,006.5 billion at end of year 2020. This was mainly due to the increase in Treasury bill holdings by Rs. 663.3 billion together with the increase in securities purchased under resale agreement by Rs. 564.8 billion. As per the decision taken by the Monetary Board at its meeting held on 24 April 2018, the prudential equity to domestic asset ratio should be 25 per cent. However, prudential equity to domestic asset ratio fell to 10.8 per cent as the end of 31 December 2021 and was 6.75 per cent at the end of May 2022. Further, according to the Section 39(b) of the Monetary Law Act, the statutory equity to domestic asset ratio should be 15 per cent. This ratio was 20.6 per cent at the end of year 2021 and negative 5.8 per cent at the end of May 2022.

(d) According to the annual financial statements of the Bank, the value of foreign assets of the Bank had decreased by 42 per cent to Rs. 798.8 billion at the end of year 2021 from Rs.1,387.5 billion at the end of year 2020. It was Rs.1,511.6 billion at the end of year 2019. According to the weekly reports published by the Bank, the net foreign assets of the Bank had started to record a negative balance of Rs.83.9 billion in August 2021. This negative balance had increased to Rs. 387.3 billion at the end of December 2021 according to the Annual Report of the Bank. Further, negative net foreign asset balance increased to Rs.1,686.2 billion as at the end of July 2022. Net foreign assets of the Bank were reported as Rs.526.8 billion as at the end of year 2020.

3. Operating Review

3.1 The Licensing, Regulation and Supervision of Companies carrying on Microfinance Business

Audit Observation	Management Comment	Recommendation
The Licensing, Regulation and Supervision of Companies carrying on Microfinance Business are carried out by the Monetary Board of the Bank under the Microfinance Act No. 06 of 2016 (Act) with effect from 15 July 2016. Companies which are accepting deposits and providing financial services mainly to low-income persons and micro enterprises (Micro Finance Business) should obtain a license under the Act. Accordingly, only four companies had obtained the licenses to carry on microfinance business from the effective date of the aforesaid Act up to 30 June 2021. Companies which are not accepting deposits but providing financial services to low-income persons and micro enterprises in the country do not require obtaining a license under the Act. Therefore, those companies are not regulated and supervised by the Monetary Board of the Bank under the Act. As a response to Auditor General Report for the year 2019, it was mentioned that a Credit Regulatory Authority will be established to license, regulate and supervise entities engaged in the business of micro finance and money lending through a separate Act and draft of the said proposed act was forwarded to the Ministry of Finance on 26 November 2019. However, it has not yet been enacted as at end of year 2021.	Microfinance and Credit Regulatory Authority is proposed to be established, to license, regulate and supervise entities engaged in the business of micro finance and money lending, through the proposed Microfinance and Credit Regulatory Authority Act (MCRA). The draft of the proposed Act, approved by the Monetary Board, was forwarded to the Ministry of Finance (MOF) on 26 November 2019. However, due to the change in the Government, a fresh approval was obtained from the Cabinet on 23.03.2021, instructing the Legal Draftsman (LD) to draft the MCRA Bill. The Bank has submitted its observations on the first draft of the MCRA Bill to the MOF on 23.11.2021. The enactment process of the proposed MCRA involves several parties, namely, the LD, the Attorney General's Department, the MOF and the Bank and therefore, is not entirely within the control of the Bank.	Need to expedite the process with the support of all parties involved.

3.2 Pension payment to the Governor of the Bank

Audit Observation	Management Comment	Recommendation
(a) The Bank had a pension scheme (old pension scheme) for employees who were recruited to the bank on or before 31.12.1997 and at the Monetary Board decision on 01.12.1997, it was decided to amend the Bank's pension Fund rules to fall in line with the government policy, offering the employees who joined the Bank's	The entitlement of a Governor to a pension, had been recognized as well back as from the year 1968 and given that it has been endorsed officially by the Hon. Attorney-General as well, and also in view of the detailed and	Need to include a minimum period of service to avail the pension benefits.

service on or after 01.01.1998 a contributory pension scheme. As per the Rule No. 3.C of the old pension Scheme, the Governor of the Bank entitled to the pension benefits until 31.12.1997.

(b) The Monetary Board at its meeting held on 08.05.2015 had decided in principle to grant approval to implement a new pension scheme for the employees of the Bank who were recruited to the Bank on or after 01.01.1998 subject to the concurrence of the prime minister and the minister of finance. The Monetary Board had approved the implementation of the new pension scheme for the expedite implementation at the meeting held on 21.05.2015 and rules of the new pension scheme were approved at the meeting held on 17.10.2016. Accordingly, the maximum pension entitlement was 74 per cent of the pension base for employees who have a service period of 42 years or more in the Bank. At the same meeting, the Monetary Board had decided to defer inclusion of the Governor's pension in to the new pension scheme rules at the request of then Governor of the Bank. Accordingly, The Governor appointed on or after 01.01.1998 was not entitled to the pension benefits of the Bank.

(c) Board at its meeting held on 30.07.2019 instructed to Director, Human Resources Department to refer the matter related to Governor's pension, to the Secretary to the President as Governor's salary and pension are matters to be determined by the appointing authority. Accordingly then Governor referred this matter for the attention of the Secretary to the President by the letter dated 15.10.2019. The Corporate Management Committee at its meeting held on 09.11.2020 had recommended to incorporate rules for pension benefits for a person appointed as the Governor of the Bank in to the rules of the new pension scheme taking into account the letter dated 02.09.2020 of the then Secretary to the President addressed evolving events outlined above, the only applicable consideration would be whether a Governor is entitled to a pension in terms of the Rules, titled the "Establishment of Rules for Pension Benefits for the Person appointed as the Governor of the Bank under the new Pension Scheme". The Attorney-General does not specify any other consideration to be present or fulfilled either in the letter of appointment or otherwise. The pension is attracted as a Governor is deemed to be an officer of the Central Bank for the purposes of a pension. This principle has been the established norm since 1968. In this vein, although the letter of appointment of one of the former Governors does not refer to a pension, nevertheless, given the clearly established general principle and proposition and the rationale identified by the Attorney-General, it clearly appears that it is the office that attracts the pension.

In the "Establishment of Rules for Pension Benefits for the Person appointed as the Governor of the Bank under the new Pension Scheme", the only consideration in the form of a disqualification, is whether there are any criminal investigations or proceedings pending against a former governor, in which event, the pension payments would be paid or suspended and where such proceedings result in a conviction, there would be a complete disentitlement.

to the Governor, which requested to take necessary steps to rectify the pension anomalies that have occurred in relation to the Post of Governor of the Bank. In terms of the Section 12 of the Monetary Law Act No. 58 of 1949 as amended, Governor shall receive such salary as may be fixed by the President. However, aforementioned letter had not contained any reference / concurrence of the President to rectify the pension anomalies in relation to the Post of Governor of the Bank as the appointing authority of the Governor is the President on the recommendation of the Minister in charge of the subject of Finance. Further, a minimum period of serving as the Governor of the Bank to entitle to the pension benefits had not been stipulated in the pension rules applicable for the Governor. Two Governors of the Bank, who held office during the periods from 2004-2006 and 2016-2019 respectively, had informed the Bank that they do not wish to avail their pension benefits offered to them.

3.3 Subscription for Treasury Bills by the Bank

Audit Observation	Management Comment	Recommendation
As per the Section 112 of the Monetary Law Act, except in the case of Treasury Bills, for which the Bank may make direct tenders, the Bank shall not subscribe to any issue of such securities or agree to purchase the unsubscribed portion of any such issue. Further, in terms of Section 90(2) of the same Act, in conducting open-market operations in Government securities, the Bank shall have regard to the need for maintaining adequate holdings of short-term securities in order to enable the Bank more readily to contract its credit if such contraction becomes necessary. Accordingly, the Bank had purchased Rs.3,423.4 billion worth of Treasury Bills (book value) during the period from March 2020 to February 2022 mainly for the purpose of bridging the fiscal deficit and to meet debt service obligation. As per the letter presented to the Governor	While the merits of minimal monetary financing or not subscribing to fund budget deficit are recognized/ reviewed, the challenging fund raising conditions warrant facilitating Treasury bills subscription by the Bank taking into account the exceptional macroeconomic conditions of the economy, the national interest and also the possible unaffordable debt servicing cost by the Government due to underperformance of fiscal targets and sharp upward adjustment in interest rates due on account of policy necessity and	Need to limit purchasing Treasury Bills by the Bank for the purpose of monetary policy.

by the Economic Research Department of the Bank on 1 August 2021, Continued Monetary financing and resultant reserve money also had threatened the domestic price stability which had adversely affected the external trade account and balance of payment through increased demand for imports despite restrictions. However, in terms of the Monetary Law Act, purchase of Treasury Bills by the Bank is permitted only for the purpose of monetary policy and not to facilitate the government to meet its debt service obligations.	increasing uncertainties. These matters have been extensively deliberated by the Monetary Board and arrangement facilitated with gradual off-loading of Central Bank holdings based on opportune market conditions.	

3.4 Maintaining a fixed exchange rate policy by the Bank

Audit Observation	Management Comment	Recommendation
(a) According to the Daily exchange rates published by the Bank, the exchange rate of the USD had been maintained at a fixed rate (Rs.202.9992) from September 2021 to 7 March 2022. However, at the Monetary Board meeting held on 18 August 2021 to review the Monetary Policy Number 6, it was mentioned that exchange rate was determined at around Rs. 199.90 per USD through a high degree of moral suasion since April 2021.	The Exchange rates mentioned in the above section are in order.	Need to maintain exchange rates at appropriate level to achieve price stability at all time.
(b) At the Monetary Board meeting held on 04 August 2021 (Meeting No.27/2021), it was mentioned that exporters were required to convert 25 per cent of their export proceeds in to rupees. But, they are reluctant to convert their export proceeds as foreign currency deposits rates are higher than that of rupee deposits and anticipation of depreciation of rupees. Further, it was highlighted the need to address the core issue of the exchange rate. However, when one of the Board members inquired from then Secretary to the Treasury the reluctance on the part of the Government to allow the exchange rate to depreciate, then Secretary to the Treasury stated that if the exchange rate is allowed to freely fluctuate, there would be a sudden and significant depreciation which would give rise to many problems. He observed that the only way to address this issue is for a sizable inflow to take place as soon as possible.	On the 1st of July 2021, the Monetary Board(MB) and the Bank made a special, comprehensive presentation to the then Minister of Finance (MOF), who was also the Prime Minister, in detail, in order to urgently address the situation pertaining to the balance of payments and other issues. At this meeting, a multi-pronged strategy consisting of specific proposals, were made to the MOF /Prime Minister. Given some of the views expressed, notwithstanding the numerous proposals and strategies, made by the Bank, only certain of them could be agreed	Need to maintain exchange rates at appropriate level to achieve price stability at all time.

The Governor of the Bank stated that the issue of the exchange rate was also discussed with the minister and minister requested a write up from the Bank to which he could use for discussions with his political colleagues to assess the political will to allow some depreciation of the rupee.	upon at the said meeting. Thereafter, at the MB meeting of held on 04/08/2021, on more than one occasion at the said meeting, two appointed Board Members, specifically stated that there is a strong case for a gradual exchange rate depreciation.
(c) At the Monetary Board meeting held on 18 August 2021, it was approved that Governor to discuss further with the government with regard to allowing the exchange rate to adjust in line with market conditions with moral suasion to limit excessive volatility. However, the decision of allowing the exchange rate to adjust in line with the market was not taken till March 2022.	A written communication dated 12/08/2021 titled “Short term macro-economic policy initiatives” was issued to the Bank by the Ministry of Finance. One of the specific measures contained in this written communication was for the Bank to instruct the selling rate for each commercial bank, to not exceed Rupees 202/= per USD. There was also a suggestion to increase the policy rates by 50 basis points. The Monetary Board informed the Minister of Finance the matters related to foreign exchange situation of the country by issuing statutory reports dated 14.09.2021, 11.11.2021, 09.12.2021, 27.01.2022 and 28.02.2022.
(d) The remittances of foreign employees which were USD 7,103.9 million in the year 2020 had declined up to USD 5,491.5 million in the year 2021. Further, foreign worker remittances during 7 months from February 2021 to August 2021 were USD 3,549.0 million and from September 2021 to March 2022 it was USD 2,049.7 million. Accordingly, it was observed that remittances received through formal channels had decreased mainly due to significant difference shown in the exchange rate in informal market as compared with the official exchange rate.	As per the minutes of the Review of the Monetary Policy Stance pertaining to the Monetary Policy Cycle No. 06 – August 2021, it is mentioned that “A key reason for the decline in officially recorded workers’ remittances could be the large disparity between the exchange rate offered by banks and the informal market”. Other possible reasons could be the significant increase in migrant workers returning to the country in 2021, possibly due to end of employment contracts, physically bringing cash with them rather than

	channeling their earnings through banks, and lower net migration during the pandemic period.	

3.5 Maintaining low interest rates by the Bank

Audit Observation	Management Comment	Recommendation
(a) The Secretary to the Treasury by a letter dated 08.04.2020 informed the Governor of the Bank that the President has instructed state banks and some other state owned enterprises/ entities to jointly invest in the treasury bonds and bills to stabilize the money market at an interest rate of 7 per cent and requested the Bank to ensure that the government security auctions to be held that no bid above these rate should be accepted that could result in the aforementioned entities incurring a loss. (b) At the meeting of the Monetary Board held on 03 April 2020, instructions were given to the Public Debt Department (PDD) to align with the Cabinet decision to the effect that "the interest rate of a Treasury Bill maturing in 364 days shall be 7 per cent" and the interest rates of the Treasury Bills maturing in 91 days and 182 days shall be determined thereupon, and that such ratios be shown in the advertisements published on the Treasury Bills. On 06 May 2020, the Monetary Board had instructed the PDD to recommend an appropriate maximum yield rates for the Treasury Bills which are maturing in 91 days and 182 days and obtain approval/concurrence of the Secretary to the Treasury or an officer nominated by him or the Minister of Finance and subsequently, to publish those rates before the auction. (c) At the Monetary Board meeting held on 04.08.2021, it was stated that having lower interest rates had resulted in to a liquidity shortage in the market and accordingly the Bank had to pump money in to the system. Therefore, some members of the Board	The Monetary Board at its meeting held on 04.08.2021 observed that due to the liquidity constraints in the money market particularly of two state banks, the Bank had to accommodate lending through the reverse repo window in addition to allocating the unsubscribed portion of respective T-bill auctions to the Bank. In both the instances the Bank pumped money into the system. There were some rupee lending by banks at exorbitant interest rates which needed to be addressed through appropriate regulatory measures. In addition, due to heavy borrowing requirement of the Government, the yields of government securities and short-term market rates showed an anomalous behaviour. Accordingly, a substantial policy response was needed to preempt the escalation of adverse inflationary expectations, to provide the required impetus to correct anomalies observed in the market interest rate structure and to stabilize the exchange rate, thus, the Bank commenced tightening the monetary policy stance in August 2021. The Monetary Board at its meeting held on 13.09.2021 decided to halt the announcement of maximum	Need to maintain rates at appropriate levels to achieve economic and price stability.

suggested that interest rates should be adjusted upwards in line with the market conditions which would address the issue of the Bank being allocated larger volume of unsubscribed treasury bills. The Bank commenced tightening the monetary policy stance in August 2021 and accordingly, the Bank increased key policy rates (Standing Deposit Facility Rate & Standing Lending Facility Rate) by 200 basis points during the period from 18.08.2021 to 07.04.2022. (50 basis points each on 18.08.2021 and 19.01.2022, 100 basis points on 03.03.2022). The Monetary Board at its meeting held on 8 April 2022, decided to increase the policy rates of the Bank by 700 basis points and another 100 basis points on 06.07.2022 with the objective of significantly tightening the Monetary Policy stance to stabilize the economy.	acceptance yield rate for Treasury bills and Treasury bonds and to revert to normal auction procedure where interest rates are determined by the supply and demand conditions in the Government securities market.

3.6 Winding up of Finance Companies

Audit Observation	Management Comment	Recommendation
Winding up process (Appointment of a liquidator) of the four finance companies whose licenses were cancelled by the Monetary Board of the Bank in the year 2018, 2019 and 2020 have not been initiated even up to the end of year 2021. A direction was made to a finance company whose license was cancelled with effect from 05 March 2018 to initiate winding up process within 30 workings days from the date of cancellation and the said company failed to initiate winding up process within the said time frame. Also, a direction was made to another finance company whose license was cancelled with effect from 25 July 2018 to initiate the winding up process within 30 workings days from the date of cancellation and the said company failed to initiate the winding up process within the said time frame.	After cancellation of licenses of the two Licensed Finance Companies (LFCs) in 2018, the Bank had discussions with Attorney General's (AG's) Department with the intention of filing petitions at commercial high courts for winding up of aforesaid companies. After the consultations had with AG's Department it was decided not to file any winding up petitions at courts until issuing new priority of claim, as filing applications for winding up prior to issue priority of claims may cause to follow Ninth Schedule of the Companies Act for winding up purposes. Minister of Finance gazetted the Finance Business (Priority of Claims in a winding up of finance company) Regulations No. 01 of 2019 on 31.05.2019 which replaces the Ninth Schedule of the Companies Act, No. 7 of 2007. Accordingly, Director of	Need to expedite the process.

	the Department of supervision of Non-bank financial institutions (D/SNBFI) had presented the petitions for winding up of the two LFCs in 2019 and 2020. Further, appropriate liquidators have already been proposed to the Commercial High Courts for the three Finance Companies for which the winding up petitions were filed by D/SNBFI. Accordingly, aforesaid delay of filing application for winding up has been now sorted out and delays were mainly due to lacuna in the law and absence of experience of handling liquidation cases of LFCs under the FBA.	

3.7 Investments made by the Departments of the Bank which handle internal funds

Audit Observation	**Management Comment**	**Recommendation**
A loss of Rs. 2,586 million was occurred as at 10.12.2018 to the funds managed by four departments of the Bank due to investment in unsecure Reverse Repo with a particular primary dealer. The total amount of investment which was reclassified as Receivable from the said primary dealer as at 18 September 2020 was Rs. 2,953.6 million.	Full provision was made for respective investments with the particular primary dealer by 2020 and hence, at present there is no impact on financial statements of respective funds. At present, the Bank has initiated legal actions to recover the due amount of Rs. 2,953.6 mn from the particular primary dealer. Further, steps also have been taken to reduce the risk of repetition of such incidences in the future.	Need to recover the loss.