

Pradeshiya Sanwardana Bank - 2024

1. Financial Statements

1.1 Opinion

The audit of the financial statements of the Pradeshiya Sanwardana Bank (the “Bank”) for the year ended 31 December 2024 comprising the statement of financial position as at 31 December 2024 and the statement of profit or loss, statement of comprehensive income, statement of changes in equity and statement of cash flows for the year then ended, and notes to the financial statements, including material accounting policy information, 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. My comments and observations which I consider should be report to Parliament appear in this report.

In my opinion, the accompanying financial statements give a true and fair view of the financial position of the Bank as at 31 December 2024, and of its financial performance and its cash flows for the year then ended in accordance with Sri Lanka Accounting Standards.

1.2 Basis for Opinion

I conducted my audit in accordance with Sri Lanka Auditing Standards (SLAuSs). 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 Management and Those Charged with Governance for the Financial Statements

Management is responsible for the preparation of financial statements that give a true and fair view in accordance with Sri Lanka Accounting Standards, and for such internal control as management 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, management 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 Sri Lanka Auditing Standards 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 Sri Lanka Auditing Standards, 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 the management.
- Conclude on the appropriateness of the management'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.

1.5 Audit Observation on the preparation of Financial Statements

1.5.1 Internal Control over the preparation of financial statements.

Audit Issue	Management Comment	Recommendation
1. It was observed that the Bank's credit classification and impairment processes involve a high level of manual adjustments. This practice may increase the risk of inconsistent or subjective classification of credit facilities and potentially leading to the understatement of Expected Credit Losses (ECL).	Due to system limitations and in order to maintain a high level of accuracy, we make necessary manual adjustments to ensure the reliability of the results.	Automate, to the extent possible, the credit classification and impairment processes to reduce reliance on manual adjustments.
2. The Bank has erroneously classified non-refinance credit facilities as refinance loans within the Core Banking System (CBS). This misclassification has occurred due to system limitations that restrict the ability to amend product classifications once initially recorded. Therefore credit facilities that were disbursed using the Bank's own funds have been inaccurately classified as refinance loans. Therefore it was further observed that this Misclassification may lead to a significant underestimation of Expected Credit Losses.	Due to system limitations in changing the product classification within CBS, certain non-refinance loan facilities had been erroneously classified as refinance facilities, which could lead to an underestimation of Expected Credit Loss. To mitigate this, actions have been taken to manually identify and adjust such loan facilities in the impairment computation.	Enhance system functionality to allow accurate product classification and prevent future misclassification of credit facilities.

1.5.2 Non-Compliance with Sri Lanka Accounting Standard

Non Compliance with the reference to particular Standard	Management Comment	Recommendation
As per the paragraph 51 of the Sri Lanka Accounting Standard on property plant & equipment (LKAS 16), "The residual value and the useful life time of the asset shall be reviewed at least at each financial year end and expectation differ from previous estimates ,the	Arrangements have been made to adhere to the Sri Lanka Accounting Standards requirements in future.	The relevant accounting standard should be followed.

changes shall be accounted in accordance with LKAS 08”. However useful life of the fully depreciated assets amounting to Rs.2,517,809,777 as at end of the year under review which are still in use had not been reviewed and accounted accordingly.

1.5.3 Accounting Policies

Audit Issue	Management Comment	Recommendation
The bank has not assigned accurate scores to the qualitative factors of different products when performing Economic Factor Adjustment (EFA) calculation and necessary subsequent changes have not been made. All qualitative factors are given a score of '1' and the same applies to all loan products. Further, scores had not been changed from year to year and not adjusted to better reflect the impact for EFA.	The bank has engaged the model validation consultant to assist with the necessary corrections to the EFA as per the requirements. These corrections will be implemented in the computation as of 30 September 2025.	Action should be taken to properly adjust EFA.

1.6 Accounts Receivable and Payable

1.6.1 Payable

Audit Issue	Management Comment	Recommendation
1. As per the outstanding Tax Assessments of the Department of Inland Revenue, there were over Rs. 6 billion tax and penalty payments as at 31 December 2024.	Additional provision of Rs. 212,281,393/- has been made under income tax expenses in financial statements pertaining to the corporate income taxes relevant to YA17/18 and YA19/20 based on the grounds of the determinations issued by the Inland Revenue Department.	Action should be taken to pay correct tax amount as determined by the Inland Revenue Department.
2. As per the Financial Statements it was observed that there was a brought forward payable balance amounting to Rs. 174,418,972 in the Payable Bonus on Annual Operating Profit - GL 225100140 which was provided for the payment of annual operating profit bonus for the year 2023. It was observed that, the board had not approved the above bonus payment.	Necessary actions will be taken to clear the provision amount pertaining to GL 225100140 subject to management decision.	Since there was no any liability to pay the bonus for the employees due to not approving by the Board, actions need to be taken to clear the payable balance.

1.6.2 Advances

Audit Issue	Management Comment	Recommendation
1. A sum of Rs. 9,187,768 relating to 06 procurement advance payments has remained in the accounts for over one year without being cleared. This issue has been continuously reported through audit queries since 2018. However, no action has been taken, and the balances remain unchanged.	One procurement has completed and advance payment have been transferred to the asset account. Others are in progress.	Action should be taken to complete the relevant procurement and clear the long outstanding advance payment balances.
2. Adequate securities are required to be obtained when granting loans and advances in order to minimize the risk of default. As per the loan master file as at 31 December 2024, the total loan portfolio of the Bank recorded an aggregated outstanding balance of Rs.183,670,036,607. Out of this, loans outstanding aggregated to Rs.1,485,985,522 are belonging to the top 25 non-performing customers of the Bank. Further review revealed that out of total loan outstanding balance relating to the top 25 non performing customers, Rs.655,653,042, or 44 percent was not secured against immovable properties. Due to the inadequacy of available securities, the recoverability of this amount is considered doubtful.	Management comment not received.	Action should be taken to ensure that adequate and proper securities are obtained for loans and advances to safeguard recoverability and minimize the risk of default.

1.7 Non-compliance with Laws, Rules, Regulations and Management Decisions etc.

Reference to Laws, Rules Regulations etc.	Non-compliance	Management Comment	Recommendation
1. <u>Banking Act</u> <u>Directions</u> i. No. 7 of 2011 dated 05 October 2011			

a)	Direction 1.2(g) of the Guideline B	Credit Risk Policies and Procedures should be consisted with the requirement for every obligor and facility to be assigned a risk rating. However, it was observed that the bank is not in compliance with the requirement of assigning a risk rating to every obligor and credit facility. Currently, risk ratings are assigned only to customers with credit facilities exceeding Rs. 5 million which are secured by immovable properties, and facilities over Rs. 3.50 million which are secured by personal guarantees or other mortgages.	A paper has been submitted to the Board of Directors for approval upon the recommendation of the Board Integrated Risk Management Committee (BIRMC). However, this issue will be rectified with the full implementation of the Loan Origination System by 31 December 2025.	Action should be taken to ensure all obligors and credit facilities are assigned a risk rating in line with the Credit Risk Policies and Procedures.
b)	Direction 2.5(b) of the Guideline B	The Bank should consider to evaluate the rating - wise distribution of borrowers in various industries, business and personal segments. The bank has not established a mechanism to evaluate the rating-wise distribution of borrowers in various industries, business and personal segments. This may result in unchecked portfolio concentrations, inaccurate risk assessments, and ineffective credit risk management practices.	The rating of borrowers is already included in the LOS system. Hence, this issue will be rectified upon the completion of the Loan Origination System implementation by 31 December 2025.	Action should be taken to complete the Loan Origination System implementation to ensure all borrower ratings are properly recorded.
ii. No. 14 of 2014 dated 26 June 2014				
a)	Direction 4.2 - Baseline Standard for Information Security Management Guideline - II	Information classification guideline of the bank shall be published in the information security policy document to support the asset owner who shall classify the information to indicate the need, priorities and expected level of	The Information Security Policy has been reviewed in alignment with the ISO 27000:2022 standard. The Information Classification Policy has been prepared and	Action should be taken to comply with the direction.

protection when handling the information. Appropriate set of procedures for labeling information shall be developed and implemented. However, it was observed that the bank has not established a comprehensive bank-wide information classification mechanism to categorize data and information based on their level of confidentiality. Even though the bank has put in place a information security policy requirements for information classification, such have not been effectively implemented due to the non-labelling of electronically maintained files/documents.

will be submitted for approval to the BIRMC and subsequently to the Board of Directors. The assignment is scheduled for completion by 30 November 2025.

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| b) Direction 6.15 - Baseline Standard for Information Security Management Guideline II | Systems shall be monitored to review administrator, operator and fault logs and information security events shall be recorded. These logs shall be used to ensure that information system problems are identified and addressed. It was observed that the bank does not have an effective procedure in place for reviewing system logs to identify potential security issues. The absence of a log analyser system significantly limits the bank's ability to systematically monitor, detect, and respond to abnormal or unauthorized activities across its IT environment. | The procurement process for a 24-hour Security Operations Center (SOC) log monitoring facility, to be operated as an outsourced service, is currently in progress. The implementation of this facility is scheduled to be completed by 31 December 2025. | Action should be taken to comply with the direction. |
| c) Direction 13.10 - Baseline Standard for Information Security | Possibilities for information leakages shall be prevented at all times. It was observed that the bank has not implemented an Information Leakage Prevention system, which is a | Information Classification Policy has been prepared and pending approval of the BIRMC and Board, scheduled for | Action should be taken to implement an Information Leakage Prevention |

Management Guideline - II	critical control required to prevent sharing or transmission of sensitive and confidential information.	completion by 30 November 2025.	system to safeguard confidential information.
iii. No. 09 of 2021 date 16 June 2021			
Direction 8.2	Licensed banks with assets below Rs. 1 Trillion shall maintain Recovery Plan from 30 June 2022 and such plans will be subjected to review during the statutory examination of the respective bank. However, it was observed that the bank has failed to establish and maintain a recovery plan as required and was unable to present such a plan for review during the Statutory Examination. The absence of an approved and up-to-date recovery plan increases the risk of delayed recovery actions and potential instability in operations.	The Bank's existing Recovery Plan is currently being updated in alignment with the approved Augmentation Plan. The updated Recovery Plan will be submitted to the next Integrated Risk Management Committee for their recommendation and subsequently to the Board for approval.	Action should be taken to finalize the updated Recovery Plan to ensure alignment with the approved Augmentation Plan.
iv. No. 13 of 2021 dated 14 September 2021			
a) Direction 4.2.5	The Board of Directors shall ensure that the Credit Policy includes a comprehensive validation policy in respect of models used for classification, recognition and measurement of credit facilities in the licensed bank including clear roles and responsibilities, validation frequency and procedures and methodologies to be used by the bank. However, it was observed that the Bank has failed to establish the above policy.	The credit policy, which includes a validation policy for models used in the classification, recognition, and measurement of credit facilities, was approved by the Board of Directors on 5 June 2025, and has been in effect since that date.	Ensure timely implementation and continuous review of Board approved credit policies to maintain effective credit risk management.

b)	Direction 4.4	License specialized banks shall not fund to recover of any credit facility provided to any borrower by the same Bank. However, it was observed that the bank has been funded to recovery of loans by issuing new loans. Ex: Awissawella and Mawaramandiya Banches.	Advises were given to the relevant branches to avoid such transactions.	Action should be taken to ensure compliance with regulations, and strengthen internal controls.
c)	Direction 10.1.2 and 10.1.3	Credit facilities which are restructured up to two times other than upgraded credit facilities shall be classified as stage 2 and credit facilities which are restructured more than two times other than upgraded credit facilities shall be classified as stage 3 under SLFRS 9. However, It was observed that the Bank has not established a mechanism to accurately identify the number of times credit facilities have been restructured and therefor failed to classify them accordingly. It was further observed that incorrect staging may lead to understatement of expected credit losses (ECLs).	Since the Core Banking System currently does not have a mechanism, information is now manually collected and reviewed monthly. This will be fully corrected by the September 2025 impairment calculation.	Establish a proper mechanism to track credit facility restructurings to ensure accurate classification and correct calculation of expected credit losses.
d)	Direction 11.1.1	Upgrading of credit facilities shall be in accordance with a policy approved by the Board of Directors, and the rationale for such upgrading shall be properly documented. Such policy at a minimum shall ensure, that the bank is satisfied with the customer's ability to service future debt obligations up to a foreseeable future. However, it was observed that	The Risk Management Department upgrades rescheduled loans per the Board-approved Upgrading Policy. The Bank has not adequately considered objective evidence of customers' ability to service future debt obligations. The Bank is reviewing its policy to address this gap.	Action should be taken to comply with the direction.

the Bank has upgraded credit facilities without adequate evidence to verify compliance with the above requirement.

v.No. 16 of 2021
date 09
December 2021

a)	Direction 4.1.2	The Board of Directors of the licensed bank shall appoint one or more Deputy Chairpersons to chair meetings of the Information Security Committee (ISC) in the absence of the Chief Executive Officer. However, it was observed that the Board of Directors of the Regional Development Bank has not appointed any Deputy Chairperson(s) to the ISC.	Management comment not received.	Action should be taken to comply with the direction.
b)	Direction 4.1.6	Information Security Committee (ISC) shall report to the Board of Directors through the Board Integrated Risk Management Committee (BIRMC) and apprise the BIRMC of its proceedings at least on a quarterly basis. However, it was observed that the ISC of the Bank has not submitted such quarterly reports to the BIRMC.	Management comment not received.	Action should be taken to ensure the ISC submits quarterly reports to the BIRMC.
c)	Direction 4.1.7	Information Security Committee (ISC) is required to meet at least once in every two months. However, it was observed that the Bank has not complied with this requirement, and only 03 ISC meetings were held during the year ended 31 December 2024, instead of the minimum 06 meetings required. This may	Management comment not received.	Action should be taken to ensure the ISC meets at least once in every two months to maintain effective oversight of information security

		impair the Committee's ability to adequately monitor and address information security matters in a timely manner.		matters.
d)	Direction 4.2.1 and 4.2.2	Licensed banks shall appoint a Chief Information Security Officer (CISO) as the executive officer responsible for the licensed bank's information security. As well the CISO shall be a member of the bank's senior management team and shall be within the immediate two layers below the level of Chief Executive Officer in the organizational structure of the licensed bank. However, it was observed that the Bank has not appointed a CISO as required.	Management comment not received.	Action should be taken to appoint a qualified CISO at the required senior management level to ensure compliance and strengthen the information security governance.
e)	Direction 4.6.5	Licensed banks shall ensure that business units responsible for technology driven banking products and services such as payment cards and electronic banking, and information technology and information security related service delivery functions are subjected to quarterly Risk and Control Self-Assessment (RCSA) process implemented and monitored by the risk management function. However, it was observed that the Bank has not implemented this direction.	Management comment not received.	Action should be taken to implement a Risk and Control Self-Assessment process on quarterly basis to ensure proper risk monitoring and compliance.
f)	Direction 4.6.6	Licensed banks shall implement an adequate technology risk management and monitoring measures including Risk and Control Self – Assessment processes for third-party service	Management comment not received.	Action should be taken to comply with the direction.

providers and agents that commensurate with the criticality and sensitivity of services carried out by such third-party service providers and agents as approved by BIRMC of the licensed bank. However, it was observed that the Bank has not implemented the BIRMC approved Risk and Control Self – Assessment processes or adequate monitoring mechanisms for its third-party service providers and agents (if any). It was further observed that, this non-compliance increases the risk of inadequate oversight over outsourced activities, potentially exposing the Bank to operational, compliance, and information security risks.

g) Direction 4.7.1	Licensed banks shall ensure that compliance with the requirements in this regulatory framework and other Central Bank Regulations relating to information security and technology risk management, the internal audit division need to check such compliance at least annually. However, it was not evidenced during the audit that the Bank's internal audit division had carried out such an assessment regarding compliance with Central Bank regulations on information security.	Management comment not received.	Ensure the internal audit division conducts annual assessments to verify compliance with Central Bank regulations.
h) Direction 5.1.1	Licensed banks shall implement a comprehensive annual training and awareness program on information security and technology risk management for Board of	Management comment not received.	Conduct structured annual training and awareness programs on information

Directors. Such training shall consist of at least one annual structured training program and one or more awareness sessions by information security and technology risk management experts every year. However, it was observed that the Bank has not conducted such a training or awareness program for its Board of Directors.

security and technology risk management for the Board of Directors as required.

i)	Direction 5.1.2	Licensed banks shall ensure that the staff of the licensed bank, agents, and third-party service providers exposed to or can potentially be exposed to critical information systems, customer data, or confidential non-customer data are trained and certified on information security. Further, the Board of Directors may exclude staff of agents and third-party service providers from the requirements, if adequate and comparable information security awareness measures have been implemented by such agents and third-party service providers. However, it was observed that the Bank has not provided the required training and certification to its all staff and has not verified whether agents and third-party service providers have implemented adequate information security awareness measures.	Management comment not received.	Action should be taken to comply with the direction.
j)	Direction 5.2.2	Licensed banks shall implement an industry standard user access and identity management system(s) to manage all users including privileged users. However, it	Management comment not received.	Action should be taken to implement an industry-standard user access and

		was observed that the Bank has not implemented such a system and this may exposes the Bank to risks related to unauthorized access, potential misuse of privileged accounts, and inadequate control over critical information systems.		identity management system.
k)	Direction 5.2.3	Privileged user access shall be provided only on “need-to-have” basis and highest level of access shall only be provided for a limited time when such access is required. However, it was observed that the Bank has not implemented this control, thereby increasing the risk of unauthorized or excessive access to critical systems, which could potentially lead to operational, security, and data integrity issues.	Management comment not received.	Action should be taken to restrict privileged user access to a “need-to-have” basis.
l)	Direction 5.2.4	Licensed banks shall conduct user access privilege reviews at least on quarterly basis for critical information systems, at least on bi-annual basis for non-critical information systems exposed to customer data and confidential non-customer data and at least on annual basis for all other information systems. However, it was observed that the Bank has conducted user access privilege reviews only on an annual basis for 12 critical information systems (except for the Core Banking System) and for 09 non-critical information systems.	Management comment not received.	Action should be taken to conduct user access privilege reviews as required to ensure proper access control.
m)	Direction 5.4.1	All electronically maintained data shall be classified based on information security	Management comment not received.	Action should be taken to comply with

sensitivity and labeled with assigned classification, as per an information classification policy approved by the Board of Directors. However, it was observed that the Bank has not complied with this direction and still had not finalized the information classification policy.

the direction.

n)	Direction 5.5.1	Customer data shall normally be protected using encryption as recommended by this direction. This requirement shall be applicable to customer data maintained with the licensed bank, agents, and third-party service providers. However, it was observed that the Bank's encryption algorithm has not yet been approved by the Board Integrated Risk Management Committee.	Management comment not received.	Action should be taken to comply with the direction.
o)	Direction 5.6.1 and 5.6.7(iii)	All licensed specialized banks that are offering electronic delivery channels other than automated teller machines (e.g., internet banking, mobile apps, customer/third-party integrations, etc.) shall implement a Security Operation Center as per the requirements in this regulatory framework. Additionally, the implementation of a Data Loss Prevention (DLP) tool is mandatory for all licensed banks. However, it was observed that the Bank has not implemented a Security Operations Center or a Data Loss Prevention tool.	Management comment not received.	Action should be taken to comply with the direction.

p)	Direction 5.7.1	Licensed banks shall have an up to date and Board of Directors approved Incident Response Plan (IRP), detailing procedures for incident escalation, remediation, recovery, and communication with internal and external stakeholders. IRP shall include specific procedures to deal with commonly known types of information security incidents, including but not limited to cyber security incidents. However, it was observed that the Incident response plan has not been still approved by the Board of Directors.	Management comment not received.	Action should be taken to comply with the direction.
q)	Direction 6.2.2 and 6.2.3	The Board of Directors on the recommendation of Board Integrated Risk Management Committee shall establish the system availability targets for each critical information system. As well BIRMC shall ensure that achievement of system availability targets of critical information systems are monitored and reported to the Board of Directors. However, it was observed that the BIRMC has not monitored and reported the achievement of system availability targets to the Board of director as per this direction.	Management comment not received.	Action should be taken to comply with the direction.
r)	Direction 7	Licensed banks shall ensure at least a minimum number of staff with eligible qualifications are employed in information security, technology risk management, and internal audit functions as required. Accordingly	Management comment not received.	Employ the required minimum number of qualified staff in relevant functions as per the

		Regional Development Bank shall have 08 qualified officers at managerial and executive level. However only 01 qualified officer is employed in the bank.		direction.
s)	Direction 8	Licensed bank shall implement following Mandatory ISO standards by International Organization for Standardization and obtain certification or assurance as outlined below, • Latest edition of ISO/IEC 27001 • Latest edition of ISO/IEC 27035 • Latest edition of ISO/IEC 22301 • Latest edition of ISO/IEC 20000 However, it was observed that the bank has not implemented and obtain certification for any of these standards.	Management comment not received.	Action should be taken to implement and obtain certification for the mandatory ISO standards to strengthen the bank's information security and operational resilience.
t)	Direction 9.9.3	Explicit customer consent shall be obtained, for exposing customer data to third-party service providers, prior to entering into a new business relationship with either new or existing customer, when a licensed bank is utilizing information system infrastructure managed or owned by third-party service providers for information systems exposed to customer data. Further, if any information system exposed to customer data is already utilizing information system infrastructure managed or owned by third-party service	Management comment not received.	Action should be taken to comply with the direction.

providers, licensed bank shall inform of such arrangement to all customers whose data are stored or processed in such information systems. Licensed banks shall seek the explicit consent of the customers whose data are stored or processed in an information system utilizing information system infrastructure owned and managed by the bank, whenever such an information system is migrated to information system infrastructure managed or owned by third-party service providers. However it was observed that the bank has not been acted accordingly.

2. Directions,
Determinations,
and Circulars
issued to Licensed
Specialized Banks
by the Central
Bank dated 02
December 2013

a) Section 3(1)(iii)	The number of directors of the board shall not be less than 7 and not more than 13. However, the board has comprised with only 6 members as at 31 December 2024.	Management comment not received.	Action should be taken to comply with the direction.
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b)	Section 3(2)(iv)	The board shall have at least three independent non-executive directors or one third of the total number of directors, whichever is higher. Nevertheless, Non-Independent Director from the General Treasury had not been appointed until 08 November 2024 for the year 2024 (previous member of the General Treasury was elected on 27 September 2023). And also, three Non-Independent Directors from each of shareholder Banks had not been appointed in the 4th quarter of 2024.	Management comment not received.	Action should be taken to comply with the direction.
c)	Section 3(1)(iii)	The board shall meet regularly and board meetings shall be held at least twelve times a year at approximately monthly intervals. However, 15 meetings were held up to 10 September 2024 and no Board meetings were conducted after that due to lack of quorum. This resulted a considerable gap without Board oversight, violating the requirement to hold meetings at least 12 times per year at approximately monthly intervals.	Management comment not received.	Action should be taken to comply with the direction.
d)	Section 3(6)(v)(e)	The Integrated Risk Management Committee shall meet at least quarterly to assess all aspects of risk management including updated business continuity plans. However, the committee has met only three times during the year 2024, and no meetings were held in the fourth quarter of the year.	Management comment not received.	Action should be taken to comply with the direction.

e)	Section 3(6)(v)(g)	The Integrated Risk Management committee shall submit a risk assessment report within a week of each meeting to the board seeking the board's views, concurrence and/or specific directions. However, the report on the Key Risk Indicators of the Bank is prepared on a monthly basis and submitted at the very next Board meeting.	Management comment not received.	Ensure the compliance with these regulations.
f)	Section 3(1)(i)(j)	It should be Periodically assessed the effectiveness of the board directors' own governance practices, including: The selection, nomination and election of directors and key management personnel; The management of conflicts of interests; and The determination of weaknesses and implementation of changes where necessary; However, it was observed that only five out of nine Board members submitted their Self-Assessment Forms for the year 2024. The incomplete submissions may affect for the poor comprehensive self-evaluation and unaddressed weaknesses in governance practices, affecting decision-making and accountability.	Management comment not received.	Ensure the compliance with these regulations.

3. Establishment
Code of the
Democratic
Socialist Republic
of Sri Lanka -
Volume II

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| a) | Sections 10:1 and 10:2 | A selected candidate for a certain post should be referred for a medical examination under a Government Medical Officer, and Form General 169 should be arranged to be sent to the Head of the Institution. However, it was observed that the Medical Form 169 was not available in 3 personnel files (File Nos. 0557, 2890, and 3272) out of the 5 personnel files of executive officers selected for audit verification. | The medical forms pertaining to two officials (Personal File Nos. 557 and 3272) are available in their respective personal files. The officer corresponding to personal file No. 2890 has already retired. Further, the highlighted medical form General – 169 is currently being used for medical examinations of the Bank. | Ensure the compliance with these regulations. |
| b) | Revision of Sub-section 22:1:1, Chapter XLVIII | A disciplinary inquiry conducted on a charge sheet issued against the misconduct of an officer should be concluded within a period of six months from the commencement of such disciplinary inquiry. This same requirement is reiterated in Section 25.8 of the Bank's Code of Disciplinary Rules, specifying a time limit of 180 days.

However, it was observed that 38 out of the total 82 disciplinary cases had remained unresolved for a period exceeding one year as at 31 December 2024.

As per the letter dated 15 May 2025 of the Assistant General Manager –Investigation, it was observed that 15 | Management comment not received. | Ensure the compliance with these regulations. |

unresolved disciplinary issues have been remained pending for more than three years and 07 issues for more than five years which are associated with a total financial loss amounting to Rs.67,617,084

4. Public
Administration
Circular

No 30/2019 dated 30 September 2019 (Revision of the sub section 13:2, Chapter XLVIII, Volume II of the Establishments Code)	An authority ordering a preliminary investigation into an act of misconduct should, at the same time that such order is issued, strictly order the officer or the Committee of Officers of the preliminary investigation to conclude such preliminary investigation within a period of two months. However, According to the disciplinary code of the bank had not mentioned a certain period to conclude the preliminary investigation and also the bank had been defined that the period of preliminary investigation as "within fair time period" in section 14.5. Based on the information provided to the audit by the Assistant General Manager – Investigations of the Bank on 15 May 2025, it was observed that preliminary investigations relating to 82 instances of disciplinary rule violations, as at 31 December 2024, had not been conducted in accordance with the relevant regulations.	Management comment not received.	Specify a clear time frame for completing preliminary investigations and ensure all investigations are conducted within the prescribed period.
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5. Operational
Manual of the
Bank

- i. The following observations have been made based on a review of 40 internal audit reports issued by the bank's internal audit unit for the year 2024.

a)	Section 2.2.8	Staff members are prohibited from maintaining more than one savings account under the same savings account code. It was observed that certain branches had not complied with this requirement. Ex: Kolonna, Vauniya, Kahawatta, Kalawana, Kurunegala, and Mawanella Branches	Management comment not received.	Action should be taken to comply with the directions given under operational manual.
b)	Section 2.3.1	It was observed that the documents required for opening savings accounts, such as mandates, KYC forms, or identity proof documents, were not available in 18 branches.	Management comment not received.	Action should be taken to comply with the directions given under operational manual.
c)	Section 6.3.3	Vault keys must be maintained under dual control and should not be kept in the custody of a single officer. However, in 11 branches, it was observed that vault keys were handled carelessly, and proper records were not maintained.	Management comment not received.	Action should be taken to comply with the directions given under operational manual.
d)	Section 6.8	A self-audit must be conducted on a daily basis by the Branch Manager or another officer-grade staff member. However, it was observed that 13 branches had not conducted daily self-audits as required.	Management comment not received.	Action should be taken to comply with the directions given under operational manual.
ii.	Section 2.2.10	Upon the confirmation of an account holder's death, all accounts under his/her name must be restricted to prevent unauthorized transactions. However, It was observed that certain branches did not comply with this requirement. Ex: 5 accounts at the Piliyandala Branch and 12 accounts at the Warakagoda Branch belonging to deceased	Corrective action has been taken now.	Action should be taken to comply with the directions given in the operational manual.

	customers, remained in active status as at the date of audit.		
iii.	Section 2.6.7 According to the prescribed procedure, the Dormant Accounts Activation Register should be maintained in the specified format, and prior to the activation of any dormant account, both an A-grade and B-grade officers are required to sign the register by giving authorization. However, during the sample audit, it was observed that the signatures of the required A-grade and B-grade officers were not present in the Dormant Accounts Activation Register. Ex: Piliyandala and Mawaramandiy Branches.	Corrective action has been taken now.	Action should be taken to comply with the directions given in the operational manual.
iv.	Section 2.6.8 If a branch intends to activate a dormant account for purposes such as recovering loan installments, charging amounts, or correcting error entries without a direct request from the customer, Form 2094 must be duly completed and submitted to the Head Office along with the Regional General Manager's (RGM) recommendation for temporary activation. However, it was observed that certain branches did not comply with this requirement. This reflects non-compliance with the prescribed procedures and increases the risk of unauthorized or irregular account activations. Ex: 2 dormant accounts at Piliyandala Branch and 4 dormant accounts at Mawaramandiya Branch.	It has now been corrected.	Action should be taken to comply with the directions given in the operational manual.

v.	Section 3.6	It was observed that cashiers transferred cash to the Reserved Vault without recording the transactions in the Reserved Cash Vault Register, as required by operational procedures.	Advice has given to follow the operational manual.	Action should be taken to comply with the directions given in the operational manual.
vi.	Section 3.8	Ex: Panadura Branch Cash had been exchanged between cashiers without being entered into the system. Cash given by the mobile cash collector, remained with the cashier without transferring to the cashier's cash. Ex: Panadura, Awissawella Branches	Advice has given to follow the instructions given and proper procedures.	Action should be taken to comply with the directions given in the operational manual.
vii.	Section 3.11.4	As per procedure, after balancing the cash at the end of the day, the relevant reports must be signed by both the Branch Manager and the Savings Officer to ensure proper verification and accountability. However, this requirement has not been complied with at several branches. Ex: Panadura, Awissawella, and Mawaramandiya Branches	Advice has given to follow the operational manual.	Action should be taken to comply with the directions given in the operational manual.

6. Internal Circulars of the Bank

i.	Office Instruction Circulars			
a)	Section 17 of 2010/10 - (Development Loans)	The branch should request the covering approvals from the Regional General Manager for the staff pawning limits. However, some instances were observed that contrary to this direction. Ex: Panadura Branch	Advice has given to follow the Circulars issued by the Bank.	Action should be taken to comply with the circular instructions.

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| b) | Section 5.3 of 2010/10 - (Development - Amended) | As per the circular, pawning articles with a physical gold Carat value below 18 should not be accepted as collateral. However, during the audit, it was observed that five pawning articles with Carat values below the required standard were accepted by the Piliyandala Branch. | The relevant officials now have signed the pawning receipt and confirmed that the Carat value was verified. | Action should be taken to comply with the circular instructions. |
| c) | Section 4(vi) of 2020-209, 2021-226 and 2024-249 | According to the stipulated conditions, loan facilities should not be granted to customers who are in default status. However, instances were observed where loans had been disbursed despite adverse credit records of the borrowers, as evident from the CRIB reports,
<ul style="list-style-type: none"> • For Loan No. 501088900010 amounting to Rs. 30 million, the primary borrower had 07 credit facilities in arrears, including 02 facilities overdue by more than 90 days, while the joint borrower had 04 credit facilities in arrears, including 01 facility overdue by more than 90 days. • For Loan No. 722088500027 amounting to Rs. 2.4 million, the borrower had arrears credit facilities totaling to Rs. 785,410. • For Loan No. 809089000003 amounting to Rs. 5 million, the second borrower had arrears credit facility of Rs. 314,716. | Agreed. Necessary actions will be taken to address this issue with a proper plan, in coordination with the branch, by 30 September 2025. | Action should be taken to comply with Circular instructions. |

ii. Office Operations Circulars 2010/05	As per requirements, the permanent address verification document of loan applicants (Form No. 702-C(i)) should be maintained in the loan files. However, it was observed that this document was not available in 15 loan files with loan value aggregating to Rs. 178 million. Further, in respect of Loan No. 243083700001 amounting to Rs. 20 million, Form No. 83, Form No. 84, and the renewed compliance report for the building construction issued by the National Building Research Organization were also not available in the loan file.	Agreed. Necessary actions will be taken to rectify this issue by 31 July 2025.	Action should be take to comply with circular instructions.
iii. Human Resource Circular	Section 3.4.5 of 2023/02 - Bank Assurance According to the relevant circular, mobile cash transported by three-wheelers or motorbikes is limited to Rs. 800,000 to ensure security and compliance with cash transit guidelines. However, it was observed that the limits were exceeded by certain branches. Ex: Awissawella and Mawaramandiya Branches.	Advice has given to follow the Circulars issued by the Bank.	Action should be taken to ensure the compliance with relevant circulars.

1.8 Non-compliance with Tax Regulations

Audit Issue	Management Comment	Recommendation
According to the Section 7 of Inland Revenue (Amendment) Act No 04 of 2023, every withholding agent who has deducted Advance Income Tax under the provisions of	The Bank was unable to submit withholding tax information to the IRD due to a lack of information generated by the	Action should be taken to rectify the issues in the Core Banking System to

section 84A shall file with the Commissioner General a quarterly statement as specified by the commissioner-General, within thirty days after the end of each quarter, ending on the thirtieth day of June, thirtieth day of September and thirty first day of December. However, the bank has failed to filed the Withholding tax returns for the year under review.

Although the bank has paid Rs.1,038,933,915 amount of Withholding tax during the year 2024, details of interest income on which the Withholding tax has been deducted and exempted interest income had not been submitted to the audit.

CBS system. However, this has already been recovered, and data is currently being processed. We will be able to upload all pending tax returns before March 31, 2025.

Exempt interest cannot be verified without using the centralized process, due to insufficient information. However, exempt interest is recorded at the branch level and it will be corrected once the reporting mechanism has been executed.

ensure that quarterly withholding tax returns are filed accurately and within the statutory deadlines.

1.9 IT General Controls

Audit Issue	Management Comment	Recommendation
1. As the bank relies on a C-Panel-based email solution provided by a third-party vendor, it associated with the following risks and inefficiencies that may impact on security, compliance, and operational controls of the bank.		
i. The bank’s current email solution lacks industry-standard security controls such as advanced spam/phishing filtering, attachment sandboxing, domain authentication and encryption for sensitive communications.	Bank has already taken the necessary actions to address specifically, in accordance with management instructions and the availability of budget, we have initiated a procurement process to replace the existing vulnerable email hosting solution.	Make necessary arrangement to strengthen the e mail security of the bank.
ii. The Bank does not maintain any backup system for its email communications and hence critical business correspondence and records are at risk in the event of accidental deletion, system failure, cyber-attacks, data corruption etc.	According to this, the bank prepared a comprehensive bid document, which was subsequently submitted to the procurement division. However, the procurement process was delayed for various reasons from time to time.	
iii Email system is managed by a third party. As a result of this the bank has limited control over some activities such as configurations,	The 1st Procurement	

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| | security policies, and data management etc. | canceled due to the bank's unfavorable financial position. |
| iv | According to the available information to the audit, the email server had been hired many years ago. It may increase the risk of email crashes or data loss. | 2 nd Procurement canceled because the lowest price solution did not meet the comprehensive email security feature. Considering all these factors, the IT division has |
| v | According to the information currently available to the audit, it has been observed that the Bank's existing email solution does not align with industry best practices and also, it was observed that this situation could be lead to severe consequences, compromising the operations of the bank, Customer trust and overall stability. | resubmitted a new proposal that combines both Email security and email hosting solutions into a single, integrated solution. |
2. Bank has implemented 03 changes to its Core banking system during the year ended 31 December 2024.
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| i. | It was observed that the individuals responsible for developing the changes were not documented. This absence of attribution results in a lack of accountability. As a result of this troubleshooting and post-implementation reviews become challenging. | The current change request form does not include a field to capture the name of the developer responsible for implementing the change. However, we will revise the existing form to include this information. | Action should be taken to implement a formal change management process with required documentation. |
| ii. | It was observed that two changes were implemented without being assigned unique reference numbers. This lack of proper identification hinders effective tracking and reconciliation of modifications, thereby increasing the risk of unauthorized or untraceable changes. | A unique identification number will be assigned to each change moving forward, which will be issued and tracked through a centralized control point. | Implement a formal change management process with required documentation. |
3. Following observations are made on terminating the Core Banking System user access created for employees.

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| i. | It was observed that 4 user accounts were accessed after the employees' official retirement dates and remained active. This situation constitutes a significant security risk, as it may result in access to sensitive systems and data by unauthorized individuals. Further, it is advisable to investigate who had logged in to the system. | The process has been expedited. The HR department send advises before the resignation or retirement date, and we terminate the user access on the next working day following the resignation or retirement date. | Implement strict user access controls to ensure that all retired user accounts are properly disabled. |
| ii | It was observed that 784 user accounts have been in the suspension status in the core banking system without any further administrative action such as termination or review. These accounts remain within the system having no activity for over a long time as early as 2013. It was observed that, if such accounts are not properly managed it may result unauthorized access and misuse of sensitive banking systems and data. | If a suspension needs to be changed to termination, the user must first be reactivated and then blocked again under the termination option. User blocking and unblocking can only be performed by authorized personnel in the IT department. | Actions should be taken to properly manage the suspension accounts. |
| iii | Trainees are provisioned with system access based on a pre-defined end date that corresponds to the anticipated duration of their training. Although access is automatically revoked upon reaching this scheduled end date, there is currently no automated or manual process in place to terminate system access for trainees who depart the bank prior to the completion of their training period. As a result of this, if trainees are early terminated, the system provides the facility to access to the system for the remaining training period. This may leads to increase access to sensitive systems and data, posing a serious risk of unauthorized access or misuse. | We have implemented a new process to deactivate trainee users who not logged in to the CBS for two months. This process is carried out once a month. | Actions should be taken to immediately revoke system access for trainees who leave the bank. |

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| iv | According to the information provided to the audit the bank has terminated 159 CBS user accounts during the year ended 31 December 2024. It was observed that there were significant delays ranging from 5 to 203 days in terminating user access to the bank's core banking system for 57 employees who had either resigned or retired. This may result in continued access to sensitive systems and data, thereby posing a serious risk of unauthorized access or potential misuse. | The user access termination process has been implemented. A new process has been implemented to deactivate trainee users who have not logged in to the CBS for two months. This process is carried out once a month. | Actions should be taken to implement a strict access termination process to ensure that user accounts in the core banking system are disabled immediately upon employee resignation or retirement. |
| v | According to the information provided to the audit, it was observed that, 20 active user accounts in the CBS that have remained unused from 01 to 08 years period. For an example, User ID 012611 which created to a trainee is remaining unused and in active status from 2014. These dormant accounts show no evidence of login activity or system usage, and there is no formal process in place to periodically review to identify such account. | The CBS system does not have a facility to identify and mark dormant users. 6 users terminated already. | Actions should be taken to introduce a formal process to regularly review all user accounts in the core banking system. |

2. Financial Review

2.1 Financial Result

The operating result of the year under review amounted to a profit of Rs. 1,275,449,488 and the corresponding profit in the preceding year amounted to Rs. 863,517,816. Therefore an improvement amounting to Rs. 411,931,672 of the financial result was observed. The reasons for the improvement are the increase of other operating income, decrease of interest expenses and the impairment reversal.

2.2 Trend Analysis of major Income and Expenditure items

Analysis of major income and expenditure items of the year under review compared with the preceding year with the percentage of increase or decrease is as follows.

Description	Variance Increase/ (Decrease) (Rs. Million)	Variance Percentage	Reason for the Variance
Interest Income	(8,310.7)	18%	Decrease of interest rates.
Interest Expense	(10,922.2)	37.3%	Decrease of interest rates on customer deposits.

2.3 Ratio Analysis

Some of the important ratio of the bank for the year under review and the preceding year together with the sector ratios are given below.

	Sector Ratios (Licensed Specialized Banks)	2024	2023
	Percentage	Percentage	Percentage
<u>Profitability Ratios</u>			
Net Profit Ratio (PAT)	6.39	3.22	1.81
Net Interest Margin	4.64	6.27	5.79
Net Interest Income on Interest Income	38.18	51.56	36.65
Non-Interest Income to Total Income	2.29	4.12	2.85
Interest Cost to Interest Income	61.82	48.44	63.35
Staff Cost to Operating Expenses	70.35	75.46	75.64
Return on Average Assets (ROA)	1.40	1.03	0.40
Return on Equity (ROE)	12.40	5.83	5.07
Earnings Per Share		2.27	1.54
<u>Asset Quality</u>			
Non Performing Advance Ratio			
- Impaired Loans (Stage 3) Ratio (%) (Net of Stage 3 impairment)	12.40	6.25	8.80
- Impairment (Stage 3) to Stage 3 Loans Ratio (%)	34.50	41.88	36.03
<u>Capital Adequacy Ratios</u>			
	Minimum Requirement		
Common Equity Tier I Capital Ratio	8.5	9.51	10.09
Total Tier I Capital Ratio	8.5	9.51	10.09
Total Capital Ratio	12.5	15.52	17.28
<u>Liquidity Ratios</u>			
Liquidity Coverage Ratio	342.40	402.00	976.00
Net Stable Funding Ratio	179.50	152.00	174.00

Following observations are made.

- i. While the Net Profit Ratio (PAT) showed an improvement from 1.81 per cent to 3.22 per cent in the year under review, it remains almost half the sector average ratio of 6.39 per cent.

- ii. Return on Equity (ROE) was at 5.83 per cent , which is less than half of the sector average ratio of 12.40 per cent , indicating a poor returns for shareholders.
- iii. Return on Assets (ROA) was although improved from 0.40 per cent to 1.03 per cent in the year under review, it remains below the sector ROA of 1.40 per cent , signaling an inefficient use of assets to generate profits.
- iv. Staff Cost to Operating Expenses was 75.5per cent in the year under review and it is above the sector average ratio of 70.30 per cent.

3. Operational Review

3.1 Management Inefficiencies

Audit Issue	Management Comment	Recommendation
1. It was observed that, inadequate budget planning/allocation for critical cyber security upgrades and lack of priority given on email security. This indicates a lack of sufficient attention and commitment at the top management to ensure the email security measures are in place to mitigate potential risks.	Corrective actions and strategic decisions have been taken.	Ensure that adequate budgetary provisions are made for critical cyber security upgrades.
2. The Grain Warehouse Project, initiated by the Ministry of Finance in 2015 with World Bank financial assistance, aims to provide storage facilities for farmers who are lacking adequate space to store their harvest and to enable them to obtain financial assistance by pledging stored crops. Five warehouses have been established in Upuldeniya, Medirigiriya, Buttala, Murunkan, and Kilinochchi, with the management services provided by the Bank. Following observations are made during the inspection of Upuldeniya and Buttala warehouses.		

Upuldeniya Warehouses

i. As per the details submitted to audit by the bank, the warehouse capacity was stated as 5,000 MTs, whereas the agreement records indicate a capacity of approximately 3,300 metric tons (MTs). However, utilization has remained significantly below the capacity during the year under review and the capacity utilization details relating to the last 4 years period are as follows.	Management comment not received.	Take necessary steps to improve warehouse utilization to achieve the expected objectives from the project and ensure accurate reporting of
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	2020	2021	2022	2023	2024
Capacity utilization (MT)	598	984	1,651	1,148	719
Utilization of capacity as a percentage (%) of 5,000 MT	11.96	19.68	33.02	22.96	14.38

storage capacity.

- ii. As per the Section 6.17 of the Agreement which the District Secretary of Anuradapura entered into with the Bank on 12 March 2015, warehouse manager is responsible for the proper maintenance of the ware house building. However, the following deficiencies were observed.

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| <p>a) Some parts of the stores had been damaged, allowing birds (pigeons) and other animals to enter. As a result, grains have been destroyed, leading to hygienic concerns and potential food contamination.</p> <p>b) According to the information made available to the audit, no proper maintenance has been carried out by the authorities since the establishment.</p> | <p>Management comment not received.</p> | <p>Ensure the warehouse manager takes prompt action to rectify the deficiencies and maintain the warehouse building in proper condition in order to achieve the expected objectives from the project.</p> |
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- iii. As per the clarifications made by the manager of the ware house related to the installed machines, following observations were made.

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| <p>a) The major machines of the warehouse, namely the 5-Ton Elevator (Dryer) , Dryer with Elevator, and Grain Cleaner, have remained idle since their installation in 2015. Accordingly, these machines have not being utilized for their intended purpose for 10 years. Furthermore, according to the information made available to the audit this situation had not been properly reported to the responsible officers, as required under Section 6.14 of the initial Agreement dated 12 March 2015. It was observed</p> | <p>Management comment not received.</p> | <p>Take immediate action to utilize the major warehouse machines effectively and ensure timely reporting of their status to the responsible officers to support proper</p> |
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that, the proper working conditions of the above machines are directly affected to the day to day functions of the warehouse.

warehouse operations.

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| b) | Although a fully equipped laboratory suitable for its intended purpose was available, most of the machines and equipments purchased and installed in 2015 including refrigerators, laboratory ovens, seed hardness testers, balances, drying ovens, grain polishers, testing huskers, seed cleaners, sieve sets, hand grinders, sample dividers, and bag closers have remained unused since installation. | Management not received | comment | Take steps to utilize the laboratory equipments effectively to achieve the objective of the project. |
| c) | As per explanations made by the manager of the warehouse, solar system was collapsed and information was not made available to the audit. However, electricity bill had been paid in fully and it was observed that the proper attention had not paid by responsible officers regarding the smooth functioning of the aforesaid system and to get the expected return. | Management not received. | comment | Action should be taken to overcome the current situation and use the system for its intended performance and returns. |
| d) | CCTV system had not been operating and repairs had not been carried out. | Management not received. | comment | Action should be taken to carry out necessary repairs as per the agreement. |
| iv. | It was observed that, contrary to the requirements of the agreements, proper maintenance records and registers had not been carried out. Specifically, essential registers such as the Stock Issuing and Receiving Register, the Register of Charges Relating to the Harvest, and the Petty Cash Register were not maintained as prescribed. | Management not received. | comment | Action should be taken to maintain all required records and registers as specified in the agreements. |

Buttala Warehouses.

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| v. | As per the details forwarded to the audit by the bank, capacity of the ware house was | Management not received | comment | Take necessary steps to |
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mentioned as 5,000 MTs whereas the capacity of the stores recorded as approximately 3,300 MTs in the agreement. However, utilization has remained significantly below the capacity during the year under review and the capacity utilization details relating to the last 4 years period are as follows.

	2020	2021	2022	2023	2024
Capacity utilization	441	652	521	891	1158
Utilization of capacity as a percentage (%) of 5,000 MT	8.82	13.04	10.42	17.82	23.16

improve warehouse utilization to achieve the expected objectives from the project and ensure accurate storage capacity.

- vi. As at the audited date of 17 July 2025, several key items were found to be malfunctioning and remained idle. The seed dryer and seed cleaner which are more essential machines to the proper functioning of the ware house had not been in operation since 25 January 2017. Further, the forklift machine had been idle since May 2025.
- Management comment not received. Arrange timely repairs or replacements of equipments to ensure smooth warehouse operations to ultimately achieve the project objectives.
- vii. Based on the information provided to the audit by the bank, it was observed that, in addition to the previously inspected warehouses, the warehouses at the Medirigiriya, Murunkan, and Kilinochchiya had also not been utilized for their intended purposes properly. The overall utilization of the capacity of these warehouses during the period from 2020–2024 was very low, and ranging between 1.75 per cent to 31.67 per cent , indicating a significant underutilization of the available capacity. Details are as follows.
- Management comment not received. Action should be taken to utilize the ware houses for their intended purpose properly.

Warehouse	Utilization of Capacity as a percentage (%) Total Capacity				
	2020	2021	2022	2023	2024
Medirigiriya	2.96	4.84	2.95	1.75	4.83
Murunkan	2.04	8.16	10.48	11.84	16.26
Kilinochchiya	25.27	31.67	25.87	26.72	30.17

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| <p>3. According to the dollar rate fluctuations in the market, it was identified an exchange loss amounting to Rs. 507,613,938.33 and an exchange gain amounting to Rs.99,416,882.43. The net impact was an exchange loss of Rs. 408,197,056 for the year ended 2024.</p> | <p>The bank's USD asset and liability exposure shows a Net Open Position of approximately USD13 million in the year 2024. Further appreciation of the LKR against the USD in 2024 resulted in an exchange loss for the bank. The bank's ALCO decided on 10 October 2024 to sell NOP so that any future losses due to exchange rate fluctuations are mitigated, which earlier resulted in a loss for the bank. Accordingly, the decision was taken by the bank to sell, USD 13.2 million on 20 November 2024. Hence, additional exchange losses will be mitigated in the future.</p> | <p>Action should be taken to improve the Foreign Currency Risk Management System.</p> |
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3.2 Operational Inefficiencies

Audit Issue	Management Comment	Recommendation
1. During the audit of five branches (Panadura, Piliyandala, Awissawella, Mawaramandiya and Warakagoda) in the year under review, following common deficiencies were observed in branch record keeping and operational controls. i. Vouchers have not properly signed by the relevant officer and the second officer, and not duly authorized by the Manager. ii. Voucher bundling register was not up to date. iii. Voucher bundles have not sealed appropriately. iv. ATM card stock book was not available or not properly maintained. v. Non availability of signatures of A Grade officers in the ATM card issuing register.	Corrective action has been taken now.	Branches should ensure that all relevant registers and stock books are, up to date, accurately maintained and properly authorized by the responsible officers.

vi.	Gift item stock book has not balanced properly and non availability of signatures of both A and B Grade officers.		
vii.	Pawning stock book was not up to date.		
viii	Deceased Accounts Register was not up to date and non availability of signatures of both A and B Grade officers.		
ix.	Non availability of signatures of authorized officers in the Cash Transport register.		
2.	It was observed that loan files had not been maintained with standardized content/index page and proper file reference numbering. As a result of this, it is difficult to systematically locate and verify critical loan documents.	Noted	Action should be taken to proper maintain of loan files
3.	It was observed that security documents for certain loans were filed in the loan files instead of being kept in safe custody. Examples of such loans include Loan Nos. 811089200001, 722088500027, 809089000003, and 305089200001.	Noted	Action should be taken to ensure the security of documents.
4.	It was observed that no emergency exits were in the certain branches. Ex: Devinuwara and Kekanadura Branches.	Management comment not received.	Action should be taken to improve the security standards in the branches.

3.3 Transactions of Contentious Nature

Audit Issue	Management Comment	Recommendation
The Bank has granted two loans aggregating to Rs.15,000,000 under loan numbers of 254083500028 and 254083500030 on 13 September 2023 and 27 September 2023 respectively to a boat Manufacture/Purchaser. It was included a condition in the respective credit facility evaluation form, stipulating that the bank should directly pay the sum to the manufacturer of the boat by cheque, or settle the amount which has already been paid by the customer after verifying the related bills and documents. The borrower has submitted a cash memo of Rs. 4,000,000 under No. B 2446 dated 08 March 2022 to prove an advance payment made to the Boat manufacture under loan No. 254083500030. Later the borrower had submitted a cash memo with the same number of B 2446, with the same amount and same information with different date of 02 October 2023 as a supporting document for a CEFT instruction for Rs.4,000,000 on 02 October 2023 under the loan No. 254083500028. Therefor audit has a reasonable doubt	Agreed. An explanation request has been made to the branch, and once received, appropriate actions will be taken before 31st August 2025.	Action should be taken to verifying the validity and authenticity of the documents before initiating any payment.

about whether this document is fictitious. It was further observed that the bank had implemented the aforesaid transaction without verifying the validity and authenticity of that document.

3.4 Under -utilization of Funds

Audit Issue	Management Comment	Recommendation
The General Ledger balance of the PEACE Project Fund stood at Rs. 44 million as at 31 December 2024, which has remained unchanged since 2015 without being utilized. This fund had been received from the Japan Bank for International Corporation (JBIC) with the objective of providing assistance for income generation activities of villagers and farmer organizations. It was further observed that under GL 505105150 – Interest Expense PEACE Project, a 2 percent interest expense has been recognized annually, despite the fund not being deployed for its intended purpose.	The irrigation Department has requested a report about this project since its inception. Accordingly, the head office requested that the respective region. We are in the process of submitting it to the Irrigation Department as soon as we have collected it from them. However, the agreement has not been signed yet, and RDB has not even received the draft document. It is expected to be signed before 30 September 2025.	Action should be taken to utilize the PEACE Project Fund for its intended purpose.

3.5 Idle or underutilized Property, Plant and Equipment

Audit Issue	Management Comment	Recommendation
According to the information made available to the audit, it was observed that 08 number of computer softwares of Head office with an aggregated value of Rs.116,583,697 have not been currently utilized by the bank.	Arrangements have been made to dispose of the said software by following bank disposal procedures.	Action should be taken to get the maximum benefit from the resources of the organization.

3.6 Procurement Management

Audit Issue	Management Comment	Recommendation
1. <u>Cloud-based email security gateway</u> The bank had initiated a procurement process to purchase a cloud-based email security gateway and published a paper advertisement on 3 June 2024 and 25 June 2024 to supply, delivery, installation, and maintenance of the solution. The Bank has conducted the procurement procedures, and forwarded the recommendations of the Technical Evaluation Committee to the Central Procurement Committee (CPC) Minor on 24 September 2024.	The CPC Minor Committee has decided to revoke the procurement by considering the high quoted price and decided to call for fresh procurement. The procurement committee decided to revoke the procurement, considering the value for money rather than the initial cost of the procurement.	It is recommended to seek possible alternatives to enhance the email security protection of the Bank.

However, the CPC Minor revoked the procurement due to budget constraints, by leaving the bank without enhanced email security protections and without seeking possible cost-effective alternatives. Thereby resources spent on tendering and evaluations of bids were uneconomical due to last minute revocation of the decision.

2. Purchasing RDB branded 3 in 1 traveling bags for Rs. 10.5 millions

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| i. As per the Section 4.2.2 of the Government Procurement Guideline 2006, Procurement Time Schedule (PTS) has not been prepared. | The bank has not prepared a PTS by considering the amount and scale of the procurement. | Action should be taken to comply with the Government Procurement Guidelines. |
| ii. As per the Section 8.9.3 of the procurement guideline, for the contracts of goods, value exceeding Rs.500,000, a formal contract shall be signed. However, it was not available such a signed contract for this order. | The Bank has signed a letter of acceptance as primary agreement with the bidder. The arrangement will be made to rectify the issue. | |

3.7 Human Resources Management

Audit Issue	Management Comment	Recommendation
1. According to Section 26 of the Pradeshiya Sanwardana Banking Act No. 41 of 2008, the Board is required to appoint the General Manager / CEO of the bank. However, as per the correspondences reviewed for the last five years after 2019, it was observed that the Board has failed to appoint a General Manager / CEO on a permanent basis who could hold office for a continuous period of at least three years, as required under Section 26(4) of the Act.	Board of Directors at the Meeting held 05 June 2025 has advised to re-advertised the post of GM/CEO.	Action should be taken to appoint a permanent General Manager / CEO in compliance with the provisions of the Act.
2. Key Positions of the Bank such as Chief Information Officer, Deputy General Manager Credit, Special Projects & Policy Implementation and Deputy General Manager Revival and Recovery were vacated and filled on acting basis during the year 2024. Positions of Chief Internal Auditor and Chief Risk Officer were vacated during the year, and the position of Chief Finance Officer also	Management comment not received.	Action should be taken to fill all vacant key positions in order to achieve long-term business objectives.

vacated and filled on acting basis. Lack of permanent leadership may affect to an effective governance and risk management. As well delays in filling critical roles could impact long-term business objectives of the Bank.

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| <p>3. According to the cadre information reviewed during the audit, there are 565 vacancies in the approved cadre as at 31 December 2024, representing a significant shortfall in staffing at all levels. This includes 194 vacancies in the Manager / Assistant Manager / Deputy Manager / Management Trainee category and 318 vacancies in Banking Assistants category. In addition, there are 875 trainees under internship, indicating reliance on temporary resources rather than filling permanent job positions. The overall vacancy level highlights inadequate manpower planning and may adversely impact on operational efficiency and service delivery of the Bank. The Bank's staff cost as a percentage of operating expenses stood at 75.5 per cent in 2024, which is significantly above the sector average of 70.30 per cent. It was further observed that filling the existing cadre vacancies is likely to increase this ratio further, which could adversely affect the profitability and may even result in operational losses.</p> | <p>Management comment not received.</p> | <p>Take necessary actions to recruit necessary manpower for the Bank in order to ensure smooth operations.</p> |
| <p>4. According to the organizational structure specified in Administration Circular No. 2021/138 dated 01 June 2021, the approved cadre for a Grade C branch is 08 officers, consisting of 01 officer from Grade 3-I, 02 officers from Grade 3-II/3-III, and 05 officers from Grade 5-I to 5-III. However, it was observed that 21 branches were operating with excess staff, while 51 branches were functioning with a shortage of 01 to 03 officers. Further, as per the circular, the post of Branch Manager in a Grade C branch should be held by a Grade 3-I Officer. Contrary to this requirement, 18 branches were functioning without a Grade 3-I Officer, whereas 25 branches had an excess of Grade 3-I Officers by 01 to 02.</p> | <p>Management comment not received.</p> | <p>Action should be taken to proper allocation of staff to ensure the smooth operation of the bank branches.</p> |

4. Accountability and Good Governance

4.1 Annual Report

Audit Issue	Management Comment	Recommendation
As per Section 3.1 of the Guidelines on Corporate Governance for State-Owned Enterprises issued under Public Enterprises Circular No. 01/2021 dated 16 November 2021, the bank is required to submit its annual report for tabling in Parliament. However, contrary to this provision, the bank has not submitted its annual reports for the years of 2022, 2023, and 2024 to tabling in the Parliament up to the date of audit.	Management comment not received	Take immediate action to submit the annual reports for 2022, 2023, and 2024 to Parliament in compliance with the circular instructions.

4.2 Strategic Plan

Audit Issue	Management Comment	Recommendation
1. As per the provisions of Section 2.3 of the “Guidelines on Corporate Governance for State Owned Enterprises” issued by the Department of Public Enterprises under the Public Enterprises Circular No. 01/2021 dated 16 November 2021, the Board of Directors is responsible for ensuring that the institution’s strategic plan is prepared to achieve its mandated objectives within the national policy framework. The finalized strategic plan, together with the action plan and annual budget, should be submitted through the Secretary of the relevant Line Ministry to the Director General, Department of Public Enterprises or the Director General, Department of National Budget, as applicable within not less than 15 days before the commencement of the ensuing year. However, the Bank has not yet prepared a strategic plan and thereby has failed to comply with this provision. 2. Instead of a strategic plan, the Bank has prepared rolling three - year Corporate Plan. While the Board approved Corporate Plans are available for the periods of 2022–2024 and 2023–2025, no plan was developed for the period of 2024–2026. Since the Corporate Plan has not been prepared for the period of 2024-2026.	Strategic planning is the critical process of the bank, and preparation of the strategic plan for 2024 has been initiated since mid of FY24 with the insights of the board of directors. However, it has taken considerable time due to the complexity and review of the process, and it has been finalized as a strategic plan for 2025-2029. The plan has been approved by the Board of Directors and sent to the relevant line ministry. Compliance with the regulatory requirements ensures a strong relationship with stakeholders, and the bank has taken steps to comply with the stipulated deadline by submitting a strategic plan, an annual action plan, and an annual budget to the line ministry. In certain circumstances, the bank was unable to comply with	Action should be taken to comply with Section 2.3 of the guideline.

regulatory requirements due to uncontrollable factors.

4.3 Annual Action Plan

Audit Issue	Management Comment	Recommendation
1. It was observed that the bank has failed to prepare and approve an Action Plan before the commencement of the year under review. The Annual Plan was approved by the Board on 14 May 2024, after almost half of the financial year had elapsed. Further it was observed that the first four months of the year resulted in the bank falling into a loss-making position.	It takes considerable time to prepare and review prior to getting the approval from the board of directors. However, each department has been pursued to achieve its targets/ tasks in view of accomplishing its targets and make decisions to avoid negative impacts on operational efficiency while considering the economic outlook of the country.	Ensure that the Annual Action Plan is prepared, reviewed, and approved by the Board before the commencement of each financial year.
2. As per the paragraph 2(a) and the Specimen provided by the “Guidelines on Corporate Governance for State Owned Enterprises”, the action plan should specify the Financial Estimates for each activity and the Time targets in months. However, the Action Plan prepared by the bank has not consisted with these requirements.	An action plan has been prepared covering all aspects of financial and non-financial aspects relevant to all departments of the bank. Hence, financial estimates for all activities cannot be measured reliably for all activities.	Action should be taken to prepare the action Plan in compliance with the applicable guidelines.

4.4 Budgetary Control

Audit Issue	Management Comment	Recommendation
Following observations are made during the audit of the annual budget of the bank.		
1. Budgeted Cash Flow Statement had not been prepared by the Bank, contrary to the provisions of Section 2.3 of the Chapter 02 of the “Guidelines on Corporate Governance for State Owned Enterprises”. Key line items in the board approved budget do not correspond with the Statement of Profit and Loss and Statement of Financial Position.	The Bank has not prepared a Budgeted Cash Flow Statement up to now, and necessary arrangements will be made to prepare and present the same in the future. Since the structure of the final accounts and MIS reporting differs in	Action should be taken to be complied with the guideline.

nature and purpose, certain variations in line items are unavoidable.

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| <p>2. It was observed that the actual figures for gross income, interest income, interest expense, fee & commission expenses, provision for loan losses, other overhead expense and levy for the year 2024 deviated substantially from the budgeted amount with the variances ranging between 18 per cent to 192 per cent.</p> | <p>The Bank acknowledges the noted deviations between budgeted and actual figures for certain line items. However, it is emphasized that these variances were primarily due to changes in external conditions such as interest rate movements, adjustments in impairment calculation methodology, and cost control measures. Despite these deviations at the line-item level, the Bank achieved an overall profit of Rs. 1.28 Bn</p> | <p>Review and strengthen the budgeting process to ensure that budgets are realistic, aligned with the bank's operational performance, and supported by accurate assumptions.</p> |
| <p>3. It was observed that the actual figures for cash & short term funds, other assets, property plant & equipment, refinance, borrowings, other liabilities and reserve as at 31 December 2024 deviated substantially from the budgeted amount with variances ranging between 17 per cent to 63 per cent.</p> | <p>compared to the budgeted Rs. 1.29 Bn, reflecting only a 1percent variance, which is considered immaterial.</p> | |
| <p>4. These significant deviations indicate that the budgeting process have not been realistic or sufficiently aligned with the bank's operational performance and may raise concerns regarding the accuracy of budgetary forecasts, effectiveness of financial planning, and adequacy of monitoring mechanisms is in place to ensure adherence to the approved financial plan.</p> | | |