

ANNUAL REPORT OF THE BOARD OF DIRECTORS

REPORTS OF DIRECTORS

The Directors of the DFCC Bank have pleasure in presenting to the members the Annual Report together with the audited Financial Statements for the year ended 31 March 2011.

The Directors' Report contains pertinent information and disclosures required under the Companies Act No. 7 of 2007 to the extent applicable to DFCC Bank, the Listing Rules of the Colombo Stock Exchange, the Banking Act (including Directions issued thereunder) and the requirements of the Sri Lanka Accounting Standards.

GENERAL

DFCC Bank is established under the Development Finance Corporation Act No. 35 of 1955. It is listed on the Colombo Stock Exchange and is licensed as a Specialised Bank under the Banking Act No. 30 of 1988 as amended.

PRINCIPAL ACTIVITIES

BANK

The principal activity of DFCC Bank includes the business of development financing. There has been no significant

change in the nature of DFCC Bank's principal activities during the year except that investment banking services were provided mainly through a 50% owned joint venture.

SUBSIDIARIES, JOINT VENTURE AND ASSOCIATES

The subsidiaries of the Bank are DFCC Consulting (Pvt) Limited, DFCC Vardhana Bank Limited (DVB), Lanka Industrial Estates Limited (LINDEL) and Synapsys Limited. Acuity Partners (Pvt) Limited is an equally-owned joint venture and National Asset Management Limited (NAMAL) is an associate company. The nature of business and the Bank's interest in these entities are set out in Page 28 and 29 of the Annual Report.

The Bank reduced its voting and non-voting shareholding in Commercial Bank of Ceylon PLC from 26.9% to 14% during the year. It ceased to be an associate company on 2 June 2010.

GOING CONCERN

The Directors are satisfied that the Bank has adequate resources to continue its operations in the future and the financial statements are prepared on the basis of a going concern. The Auditors have declared the Bank solvent after the payment of the proposed final dividend.

FINANCIAL STATEMENTS

The Financial Statements of the Bank and the Group of Companies are given on pages 85 to 90 of the Annual Report. They have been prepared in conformity with the requirements of the Sri Lanka Accounting Standards, the Banking Act and other applicable statutory and regulatory requirements.

REVIEW OF BUSINESS OF THE YEAR

The Chairman's Statement, Chief Executive's Report and the Management Discussions and Analysis give details of the operations of the Bank and the Group and the key strategies that were adopted during the year under review.

PROFIT AND APPROPRIATION

Year ended 31 March 2011	(Rs '000)
Retained profit on 31 March 2010	992,321
Previous year dividend approved on 30 June 2010	794,452
Unappropriated profit on 31 March 2010	197,869
Profit after tax of the Bank	7,137,451
Total available for appropriations	7,335,320

Appropriations:

Transfer to:	
Reserve Fund (statutory requirement)	360,000
Investment Fund (statutory requirement)	53,600
General Reserve	2,000,000
Interim dividend declared on 31 March 2011	1,854,682
Final dividend recommended for financial year ended 31 March 2011	794,651
Unappropriated profit on 31 March 2011	2,272,387

ACCOUNTING POLICIES

The accounting policies adopted in the preparation of the financial statements of the Bank and the Group are stated on pages 91 to 104 of the Annual Report. There were no significant changes to the Accounting Policies of the Bank in the year under review.

AUDITOR'S REPORT

The Auditor's Report on the financial statements, which is unqualified, is given on page 84.

REAPPOINTMENT OF AUDITORS

The present Auditors, Messrs KPMG Ford, Rhodes, Thornton & Co. have expressed their willingness to continue as Auditors of DFCC Bank for the next financial year ending 31 March 2012. The Audit Committee has reviewed the effectiveness and the relationship with the Bank including the fees paid to the Auditors and have concluded that they are suitable to continue in office. The Directors are satisfied that based on the written representation made by the Auditors, they have no relationship or interest with the Bank or with any of its subsidiaries which would impair the Auditor's independence. A Resolution pertaining to their reappointment and authorising the Directors to determine their remuneration will be proposed at the Annual General Meeting for adoption.

THE BOARD OF DIRECTORS

The Board of Directors of the Bank consist of ten Directors with wide knowledge and experience in the fields of banking and finance, trade, commerce, manufacturing, services and law. Profiles of the Directors are given in pages 20 to 23. The following are the present Directors of the Bank categorised in accordance with criteria specified in Direction No. 12 of 2007 issued by the Central Bank of Sri Lanka.

NON-EXECUTIVE DIRECTORS

Mr J M S Brito (Chairman)
Ms H M N S Gunawardana -
Government Director

INDEPENDENT NON-EXECUTIVE DIRECTORS

Mr S N P Palihena - Senior Director
Mr A S Abeyewardene
Mr T K Bandaranayake
Mr G K Dayasri
Mr C R Jansz
Mr C P R Perera
Mr R B Thambiyah
Ms S R Thambiyah - Alternate to
Mr R B Thambiyah

EXECUTIVE DIRECTOR

Mr A N Fonseka - CEO and Ex-Officio
Director

Mr Brito does not meet the criteria set out in the Direction to be designated an Independent Director by virtue of his being a director of the subsidiary, DFCC Vardhana Bank Limited. Mrs Gunawardana represents a specific stakeholder. Mr Abeyewardene qualified as an Independent Director on 25 February 2011 on his relinquishing office as a Director in an associate company.

RESIGNATION AND APPOINTMENT OF DIRECTORS

The following Directors resigned from the Board during the year on the dates shown:

Mr A M de S Jayaratne - 30 April 2010
Mr D S Weerakkody - 2 June 2010
Mr T Caglayan - 30 June 2010
Dr (Mrs) Damitha de Zoysa - 12 July 2010

The Directors record their appreciation for the contributions made by them during their tenure as Directors.

Mr T K Bandaranayake (who was an Alternate Director) was appointed as a Director with effect from 30 June 2010. Mr R B Thambiyah and Mr C R Jansz were appointed as Directors on 28 July 2010. Mrs H M N S Gunawardana was appointed as the Government Director on 4 August 2010. Messrs T K Bandaranayake, R B Thambiyah and C R Jansz will retire in terms of Regulation No. 90 of the DFCC Regulations and are offering themselves for re-election at the Annual General Meeting. The Nomination Committee has recommended their re-election and the Board having concluded that they are fit and proper persons to be Directors in terms of the provisions of the Banking Act, unanimously endorse the recommendation of the Nomination Committee.

SECRETARY TO THE BOARD

Ms A Withana was appointed as the Secretary to the Board with effect from 25 May 2011 to succeed Mr T Wijemanna who is due to retire from the Bank shortly. The Directors thank Mr Wijemanna for the services rendered during the past 17 years.

RETIREMENT OF DIRECTORS

The Director retiring by rotation in Terms of Regulation No. 87 of the DFCC Regulations is Mr C P R Perera. He is not offering himself for re-election. The Directors thank him for the valuable contribution made by him during his tenure as a Director since 2005.

DIRECTORS' REMUNERATION

The Director's remuneration for the financial year ended 31 March 2011 is given in Note 18 of the financial statements. Mr G K Dayasri has opted not to receive any remuneration as a Director. The directors record their appreciation for the honorary services provided by Mr Dayasri.

DIRECTORS' MEETINGS

The Bank held 14 Board Meetings during the financial year. The attendance of Directors is shown in the Table on page 60 of the Annual Report.

DIRECTORS' INTEREST IN SHARES AND DEBENTURES

Mr A N Fonseka, in his capacity as Chief Executive held 34,008 options as at 31 March 2011 (17,004 as at 31 March 2010). The increase in the number was due to the adjustment made in accordance with the approved scheme arising from the bonus issue of shares during the year. Mr Fonseka has not exercised options on any shares during the financial year 2010/11.

No other Director directly or indirectly holds options or debentures of DFCC Bank.

Directors' interest in shares are given in Table 1.

DIRECTORS' INTERESTS IN TRANSACTIONS WITH THE BANK

All Directors have complied with Section 9 (6) of the DFCC Bank Act and declared any interest in transactions or proposed transactions with the Bank and all such transactions have been approved unanimously by the other Directors of the Bank.

Table 1
Directors' Interest in Shares

	No. of Shares ¹ as at 31 March 2011	No. of Shares ¹ as at 31 March 2010
Abeyewardene, A S	10,380	1,190
Bandaranayake, T K	1,478	739
Brito, J M S	18,760	9,380
Caglayan, T ²	-	Nil
Dayasri, G K	1,036	518
De Zoysa, Dr Mrs A D N ²	-	Nil
Fonseka, A N	107,998	66,499
Gunawardana, Ms H M N S	Nil	Nil
Jansz C R	1,000	Nil
Jayarathne, A M de S ²	-	750
Palihena, S N P	10,000	5,000
Perera, C P R	20,000	13,000
Thambiayah R B	211,200	49,900
Thambiayah Ms S R	Nil	Nil
Weerakkody, D S ²	-	12,844

¹ Directors' shareholding includes shares held by the spouse and children under 18 years of age

² Not Directors as at 31 March 2011

The Directors' interest in transactions with entities/persons (other than subsidiaries, joint ventures and associates) are listed under each Director for the year ended 31 March 2011 are given in Table 2:

Table 2
Directors' Interest in Transactions

	Rs '000
Mr J M S Brito	
Aitken Spence PLC	
Aitken Spence Printing (Pvt) Limited	
Browns Beach Hotels PLC	
Elevators (Pvt) Limited	
Aggregate amount of credit facilities approved	700,000
Aggregate amount of payments made for services	819
Mr A N Fonseka	
Lanka Ventures PLC	
Colombo Stock Exchange	
Central Depository Systems Limited	
Mrs R D Fonseka	
Aggregate amount of credit facilities approved	200,000
Aggregate amount of payments made for services/rent	3,462
Mr C R Jansz	
Lanka Bell (Pvt) Limited	
Aggregate amount of payments made for services	38
Mr R B Thambiyah	
Royal Porcelain (Pvt) Limited	
Aggregate amount of credit facilities approved	150,000

Messrs J M S Brito, A N Fonseka and A S Abeyewardene are or have been Chairman/Director of one or more of the subsidiaries, joint venture or associate companies. Details of transactions with subsidiaries, joint venture and associate companies are disclosed in Note 62 in the Notes to the financial statements.

BOARD COMMITTEES

The following are the members of the committees of the Board. Changes to the composition during the year are noted in the respective Committee Reports in the Annual Report.

AUDIT COMMITTEE

Mr T K Bandaranayake (Chairman)
Mr S N P Palihena
Mr. A S Abeyewardene

CREDIT COMMITTEE

Mr S N P Palihena (Chairman)
Mr A N Fonseka (Chief Executive)
Mrs H M N S Gunawardana

HUMAN RESOURCES & REMUNERATION COMMITTEE

Mr J M S Brito (Chairman)
Mr C P R Perera
Mr G K Dayasri

NOMINATION COMMITTEE

Mr R B Thambiyah (Chairman)
Mr J M S Brito
Mr C R Jansz

INTEGRATED RISK MANAGEMENT COMMITTEE

Mr J M S Brito (Chairman)
Mr A S Abeyewardene
Mr S N P Palihena
Mr A N Fonseka (Chief Executive)

The Heads of key risk assuming units, the Head of Risk Management, the Chief Financial Officer and the Head of Internal Audit are also members of this Committee.

In addition, from time to time the Board appoints committees to deal with specific matters. The Board also invites external advisers and Key Management Personnel to serve on some of the committees as and when necessary.

Further details relating to the committees are given in the section on Corporate Governance and the Committee Reports.

DIVIDEND

The Bank paid an interim dividend of Rs7 per share on 27 April 2011. In addition the Directors have recommended for approval by shareholders at the Annual General Meeting the payment of a final dividend of Rs3 per share, being the same as the final dividend paid in the previous year after adjusting for the one for one bonus issue of shares during the year under review. The total dividend for the year will amount to approximately Rs 2,650 million (Rs794 million in the previous year), which amounts to 38% of the Bank's distributable profit.

The Directors unanimously declare that, the Bank will satisfy the solvency test stipulated in Section 57 of the Companies Act No. 7 of 2007 immediately after the final dividend payment is made and have obtained a certificate of solvency from its Auditor.

PROPERTY, PLANT & EQUIPMENT AND LEASEHOLD PROPERTY

The total expenditure on acquisition of property, plant & equipment during the year amounted to Rs218 million. Acquisition of intangible assets amounted to Rs13 million. Details of these are given in the Notes 40 and 41 to the financial statements.

The information on market value of freehold properties are given in Note 41 to the financial statements.

RESERVES

Total revenue reserves augmented by the annual appropriation and retained profit amounted to Rs2,068 million.

SHARE CAPITAL AND SUBORDINATED DEBENTURES

The Bank issued bonus shares in the proportion of 1 new share for each existing share on 1 November 2010 by capitalising reserves. Consequent to this issue and the options exercised by the employees during this financial year, the total share capital as at 31 March 2011 was Rs2,649 million consisting of 264,883,768 shares of Rs10 each. Further information is given on page 135. The DFCC Bank Act No 35 of 1955 mandates a par value of Rs10 per share. The Stated Capital, if computed in accordance with the requirements of the Companies Act No. 7 of 2007 amounts to Rs4,703 million.

SHARE INFORMATION

Information relating to earnings, net asset and market value per share are given in page 156 of the Annual Report and also contains information pertaining to the share trading during that period.

SHAREHOLDERS

As at 31 March 2011 there were 9,810 registered shareholders and the distribution is indicated on page 157. The 20 largest shareholders as at 31 March 2011 are listed on page 158.

EMPLOYMENT & REMUNERATION POLICIES

The policy of DFCC Bank is to develop and maintain a dedicated and highly motivated group of employees who are committed to creating sustainable value through effective risk management and high quality service while

supporting public and private sector in its development efforts within the ambit of the DFCC Bank Act. The Bank continuously invests in training and development of its staff to meet these objectives. DFCC Bank is an equal opportunity employer. Remuneration of employees consists of fixed and variable payments. Annual increments and variable pay awards are based on the performance of the Bank and the individual. It is the Bank's policy to fix remuneration at a level which will attract, motivate and retain high quality employees. A remuneration survey is conducted once in three years, in order to appropriately benchmark the Bank's remuneration levels and policies with those in the banking and other competing private sector institutions.

EMPLOYEE SHARE OPTION PLAN (ESOP)

The last grant under the ESOP approved by shareholders was made in 2006. The exercise period of these grant expires on 2 July 2011. As at 31 March 2011, there were 228,086 unexercised options at an exercise price of Rs58.73 per share after adjusting for the bonus issue of shares during the financial year.

STATUTORY PAYMENTS

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

COMPLIANCE WITH LAWS, REGULATIONS AND PRUDENTIAL REQUIREMENTS

The Bank has not engaged in any activities contravening the laws and regulations and has complied with prudential requirements. The Directors obtain quarterly, a confirmation report from the Management with regard to compliance with laws, regulations and prudential requirements.

POST BALANCE SHEET EVENTS

Subsequent to the date of the Balance Sheet no circumstances have arisen which would require adjustments to the accounts. Significant post Balance Sheet events which in the opinion of Directors require disclosure are described in Note 64 to the financial statements.

The Bank has been granted approval by the Monetary Board to acquire up to 100% and to functionally manage DVB. This will help the Bank and DVB to further enhance synergy and operate as a single economic entity in the future.

CORPORATE GOVERNANCE

The Directors place great emphasis on following internationally accepted good corporate governance practices and principles. Systems and procedures are in place in order to satisfy good governance requirements.

The Directors' have obtained External Auditor's assurance on effectiveness of the internal control mechanism and compliance with the Direction 12 of 2007 of the Central Bank of Sri Lanka on Corporate Governance.

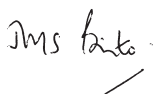
Details of governance practices and the required disclosure are given in pages 59 to 65.

Rule 3 (8) of the Direction No. 12 of 2007 on Corporate Governance for Licensed Specialised Banks in Sri Lanka prescribe disclosure in the Annual Report. These disclosures have been made in this Annual Report as depicted in the Table given below:

The Table below provides cross references to facilitate easy reference.

Reference to Rule	Requirement	Reference to Annual Report
3 (8) (i)	Financial statements on prescribed format	Financial statements on pages 91 to 104
3 (8) (ii) (a)	Affirmative assurance of compliance with accounting standards and requirements	Directors' Responsibility Statement on page 82
3 (8) (ii) (b)	Affirmative assurance of the integrity of financial reporting system	Directors' Statement of Internal Control on pages 73 to 75
3 (8) (ii) (c)	External Auditors certification on the effectiveness of internal control	Corporate Governance report on page 59
3 (8) (ii) (d)	Information on Directors	Page 20
3 (8) (ii) (d)	Remuneration of Directors	Notes on the financial statements 18
3 (8) (ii) (e)	Net accommodation granted to each category of related party	Corporate Governance Report on page 59
3 (8) (ii) (f)	Compensation and other transactions with key management personnel	Notes on the financial statements 62.6.2
3 (8) (ii) (g)	External Auditors certification on Corporate Governance	Corporate Governance report on page 59
3 (8) (ii) (h)	Compliance with prudential requirements and regulations	This report

For and on behalf of the Board of Directors,



JMS Brito
Chairman



AN Fonseka
Ex-Officio Director &
Chief Executive



Ms A Withana
Secretary to the Board

30 May 2011