

Report of the Board Integrated Risk Management Committee

Composition of Board Integrated Risk Management Committee (BIRMC)

During the financial year ended December 2018, there was no change in the composition of Board Integrated Risk Management Committee (BIRMC) of DFCC Bank except for the resignation of the Chief Risk Officer (CRO), P Gamage in August 2018. A Goonesekere was appointed as the new CRO from September 2018. BIRMC consists of three Non-Executive Directors and one Executive Director as at 31 December 2018. The Chief Risk Officer, who has the voting power, functions as the Secretary to the Committee. Heads of key functional areas such as Lending, Finance, Treasury, Operations, Information Technology, Internal Audit and Compliance attend the meetings on invitation. The membership of the BIRMC as at 31 December 2018 was as follows:

- T Dharmarajah – Chairman of the Committee/ Non-Executive Director
- L H A L Silva – Executive Director/Chief Executive Officer
- V J Senaratne – Non-Executive Director
- L K A H Fernando – Non-Executive Director
- A Goonesekere – Group Chief Risk Officer

Charter and the responsibilities of the BIRMC

The approved Charter for the BIRMC stipulates authority, structure, responsibilities and tasks of BIRMC. As per its Charter, the primary responsibilities of BIRMC are to review and ensure;

- A. Integrity and adequacy of the risk management function of the Bank
- B. Adequacy of the Bank's capital and its allocation
- C. Risk exposures and risk profiles of DFCC Bank are within acceptable parameters and to make recommendations to the Board of Directors on any action required;

- D. The adequacy and effectiveness of the Management Committees through a set of defined tools.
- E. Availability of a comprehensive and updated set of risk policies and guidelines covering overall operations of the Group.
- F. The compliance of the Group's operations with relevant laws, regulations and standards including the adherence to the CBSL Direction on Corporate Governance.

The process through which the BIRMC discharges its responsibilities is detailed in the Risk Management section of this Annual Report.

BIRMC meetings

BIRMC meets on a quarterly basis. Accordingly, DFCC Bank convened four BIRMC meetings during 2018. The attendance of members is listed on page 96 of the Annual Report. The Committee continued to review policy frameworks, risk management strategies, risk capital position, key risk indicators and top and emerging risks at these meetings and was satisfied that the risk exposures of the Bank and the Group were being appropriately managed. During the financial year, the following key initiatives were achieved by the Committee:

- A. Reviewed and approved the Internal Capital Adequacy Assessment Process (ICAAP) of DFCC Bank, which was a regulatory requirement with effect from January 2014. BIRMC took several key decisions on the capital management based on the outcome revealed by the ICAAP. They included recommending an Issue of a Basel III compliant convertible debt of Rs. 5 to 7 Bn in order to raise total capital base and to classify 5% ownership of the Commercial Bank investment as "Fair Value through P&L" under IFRS 9 and to sell at an appropriate price and time based on market conditions in order to enhance the Tier 1 capital. BIRMC will continue monitoring and proposing future capital requirements as per the Bank's growth targets for the next few years.
- B. In relation to the Management of compliance risk, compliance risk indicators with different risk scales were reviewed and specific areas of focus were recognised based on the possible impact and the probability of occurrence.

- C. Risk controls and monitoring tools were further improved with revisions to the overall risk limits system of the Bank from time to time and new advisory limits were put in place as trigger limits as required.
- D. The Committee approved the revisions of credit rating model for leasing exposures subsequent to an external validation of the model. This revision focused on recognising the borrower risk profile more effectively thereby reducing the subjectivity in assigning the scores for the model parameters. These changes have been implemented in the Bank during the year. Further, the Committee approved a new rating model for the credit card exposures.
- E. The Committee reviewed the Probability of Default (PD) based on the rating grades, Loss Given Default (LGD) for facilities and technical validation results for the credit rating models. These credit risk parameters are used in credit appraisal process, credit pricing and risk management.
- F. The annual review of effectiveness and adequacy of the Management Committees was conducted by the BIRMC during the first quarter of 2018. The review results were shared with the respective committees for necessary improvements.
- G. Reviewed and approved all the new products and redesign of any existing products of the Bank while taking both business and risk management perspective.
- H. Reviewed and implemented the CBSL recommendations based on the examination report requirements in relation to the integrated risk management function of the Bank.
- I. Having duly recognised the trends in increasing threats on systems and information security, the committee paid increased attention by reviewing the adequacy of the security in information systems and closely monitoring the action plans and implementation of new projects for further

improving information systems security in the Bank. The fraud risk management procedures were further strengthened.

New risk management policies and guidelines were introduced covering agency banking arrangements and treasury middle office operations in relation to voice recording during the financial year, while all existing risk policies and practices were reviewed by the Committee in line with the Bank specific requirements, industry dynamics and regulatory specifications.

Reporting

The proceedings of the BIRMC meetings are reported to the Board through submission of the meeting minutes. Monthly Top and Emerging Risks and other specific matters are submitted separately for the Board's information. The recommendations made by the BIRMC during the year under review were duly approved by the Board.



T Dharmarajah

Chairman – Board Integrated Risk Management Committee

18 February 2019