

Report of the Board Integrated Risk Management Committee

Composition of Board Integrated Risk Management Committee (BIRMC)

During the financial year ended December 2017, the composition of Board Integrated Risk Management Committee (BIRMC) of DFCC Bank was changed with the change of Chairman and the other Non-Executive Directors due to the retirement of some of the Directors and as recommended by the Board of Directors. L N de S Wijeyeratne (Non-Executive Director of DFCC Bank), the Chairman of BIRMC, on his retirement handed over the responsibilities to T Dharmarajah (Non-Executive Director of DFCC Bank), appointing him as the new Chairman of the Committee from November 2017. Further, Ms V J Senaratne and Ms L K A H Fernando were appointed as members representing Non-Executive Directors, while K D N R Asoka and P M B Fernando retired from the membership during the year. H A Ariyaratne was in membership for the first meeting in 2017.

There are three Non-Executive Directors and an Executive Director as at 31 December 2017. The Group 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 2017 was as follows:

- T Dharmarajah – Chairman of the Committee/ Non-Executive Director of DFCC Bank
- L H A L Silva – Executive Director/Chief Executive Officer of DFCC Bank
- Ms V J Senaratne – Non-Executive Director of DFCC Bank
- Ms L K A H Fernando – Non-Executive Director of DFCC Bank
- P Gamage – 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. Review 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 2017. The attendance of members is listed on page 113 of this Annual Report. The Committee continued to review policy frameworks, risk management strategies, risk capital position and key risk indicators 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 taking steps to enhance retained earnings by considering options such as reducing dividend payout and issuing scrip dividends. However, ICAAP did not indicate any additional capital infusion requirement for 2017. 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 as required.
- d. The Committee approved the revisions of credit rating models for corporate exposures subsequent to an external validation of the model. This revision focused on recognising the borrower risk profile in a better approach and 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 retail exposures as well.
- 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 2017. The review results were shared with the respective committees for necessary improvements.
- g. Reviewed and approved certain new products and redesign of certain existing products of the Bank while taking both business and risk management perspective.
- h. Reviewed 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.

Several new risk management policies and guidelines were introduced 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. Top and Emerging Risks and other specific matters are submitted separately for the Board's approval. The recommendations made by the BIRMC during the year under review were approved by the Board.



T Dharmarajah

Chairman – Board Integrated Risk Management Committee

19 February 2018