

An overview of Corporate Governance Laws and Regulations applicable to the Banking Industry in Sri Lanka

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Abstract

The term "corporate governance" built up its audience post-financial crisis at the beginning of the 21st century due to the common belief that good corporate governance standards lead to stability in the financial system, which is one of the key factors of a healthy society. Pursuant to this financial crisis, financial regulators in Sri Lanka also came up with certain minimum standards on corporate governance applicable to firms and companies. In Sri Lanka there are two types of banks; Licensed Commercial Banks (LCBs) and Licensed Specialized Banks (LSBs). These two types of banks control Sri Lanka's financial system and represent the largest portion of its total assets. The banking sector regulator, the Central Bank of Sri Lanka (CBSL), introduced key regulations on corporate governance in 2007 as a preliminary step towards banking sector stability. Also, banks as limited liability companies are also governed by various other corporate governance standards introduced by institutions like the Colombo Stock Exchange (CSE) and the Institute of Chartered Accountants of Sri Lanka (ICASL) etc. This paper intends to discuss the history of corporate governance in Sri Lanka and expose and examine the corporate governance rules, regulations, and codes and their primary objectives that are applicable to the Sri Lankan banking industry. The data have been extracted carefully by perusing the codified laws and regulations in the country. This article will help the readers to acquire knowledge on the corporate governance regime of the banking industry in Sri Lanka.

Key Words: Sri Lanka; Corporate Governance; Bank ;Licensed Commercial Banks; Licensed Specialized Banks

1. Introduction

Until the Bank of Ceylon was founded in 1939 following the approval of the State Council of Ceylon in 1934, banks and banking were not exactly common terminology among Sri Lankans. Up until 1948, Sri Lanka's monetary policy was governed by the Currency Board System, which was created in accordance with the Paper Currency Ordinance No. 32 of 1884. With technical support from the Federal Reserves of the USA, the Central Bank of Ceylon (later renamed the Central Bank of Sri Lanka) was established under the Monetary Law Act No. 58 of 1949. The banking sector in Sri Lanka has grown and deepened as a result of the financial sector's expansion over the last few decades. Currently, Sri Lanka has 26 banks, making it a financial powerhouse (www.boc.lk,2023).

According to the Banking Act No. 30 of 1988 of Sri Lanka, there are two types of banks.

1. Licensed Commercial Banks
2. Licensed Specialized Banks

The Sri Lankan banking system has changed from conventional, traditional banking to much more sophisticated yet complicated banking transactions, opening the door to more risk within the last four to five decades. Accordingly, from money deposits and lending it has widened to investment banking, pawnbroking, leasing and hire purchase to cryptocurrency transactions, mobile banking etc. These complicated transactions have opened the doors of banks to more risk than ever (www.cbsl.gov.lk,2023)

With the financial crisis at the beginning of the 20th century, the discussion of good governance for banks came into play. Major financial firms like "Lehman Brothers," "Bank of New England," "Freddie Mac," "Royal Bank of Scotland," and "AIG," among others, collapsed around the start of the twenty-first century, sparking a global financial crisis (Grantham, 2020). In order to prevent future financial-related problems, there has been a considerable surge in interest in corporate governance among regulators and the financial sector since the financial crisis. Numerous publications, seminars, and other pieces of literature on the subject demonstrate how popular "corporate governance" is in the financial sector even today (Hassan & Atha Mbawa, 2021).

What is Corporate Governance?

The English word "governance" comes from the Greek word "kubernaein," which means "steering" (Nelson, 2017). The concept of "corporate governance" is, nevertheless, a relatively new one (Manta, 2018). Due to the term's complexity, it has been defined in a variety of contexts, including but not limited to its legal aspect, scholarly aspect, and practical aspect. Nevertheless, in plain English, "corporate governance in a business environment refers to the system of rules, policies, and processes by which the corporations are directed and controlled" (Chen, 2021).

History and Evolution of Corporate Governance in Sri Lanka

Since the Portuguese invasion of Sri Lanka in 1505, the country has been a colony. After gaining independence from the British in 1948, the colonization era came to an end. During these years, the country was dominated for 443 years by the Portuguese, Dutch, and British (Tambimuttu, 2009). The country did not receive any of the Portuguese laws or legal framework. However, the Dutch were quite eager to impose their legislation on the nation. They dominated the country's coastal regions while Sri Lankan rulers ruled the country's interior highlands (Kingdom of Kandy). Dutch law significantly influenced the legal framework of the country (Cooray, 2009).

The Legal Framework of Corporate Governance in Sri Lanka (General)

"Ordinance of Civil Law No. 05 of 1852" was introduced in 1852 to restrict the application of Kandyan law and to apply the Law of England to all business transactions in Sri Lanka (Wickremasinghe, 2018). As a result, British models and procedures had a significant influence on corporate governance practices in Sri Lanka. Sri Lanka's corporate governance model is mostly based on the "Anglo-Saxon Model of Corporate Governance", the corporate governance model used in England. Following the end of the British administration in 1948, a number of local businesses were established using the "Anglo-Saxon model," despite professional bias against this approach (Senaratne, 2011).

With respect to share trading, the "Joint Stock Companies Ordinance No. 4 of 1861" was subsequently passed. Furthermore, the "Share Brokers Association" was established in the year 1896, and it changed its name to the "Colombo Brokers Association" in 1904. In 1938, "Companies Ordinance No. 51 of 1938" was developed

(www.cse.lk, 2023). In compliance with the aforementioned Companies Ordinance, the Registrar of Companies department was set up to assist firms established in Sri Lanka (www.drc.gov.lk, 2023).

There were several improvements to the governance structure post-adoption of free economic policy in 1977. The companies act No. 17 of 1982 was incorporated to regulate several local and foreign corporate bodies that were established post-free economic policy. It amended and consolidated laws relating to companies. It is quite a lengthy and comprehensive enactment which discusses several corporate governance requirements such as disclosures, responsibilities of directors, audit procedures, shareholder meetings etc. (Wickremasinghe,2018).

Colombo Securities Exchange (GTE) Ltd was established in 1985 after joining the Colombo Brokers' Association and the Stock Brokers' Association. It was a limited company by guarantee licensed under the provisions of Sri Lanka's Securities and Exchange Commission and registered as a company under the Companies Act No. 17 of 1982. Later, this became the Colombo Stock Exchange (CSE), and it now plays a significant role in making regulations that are applicable to listed companies and that enhance their governance structures (Wickremasinghe,2018).

In order to regulate Sri Lanka's securities market, the Securities and Exchange Commission of Sri Lanka Act No. 36 of 1987 was passed in 1987. It was passed in order to manage corporations for each unit trust, license stock exchanges, register market intermediaries, create a compensation fund, and deal with issues that are related to or incidental to those purposes. This act was amended several times, particularly in the year 1991,2003,2009 and very recently in 2021. The objective of these amendments was to improve the governance structure of the securities market and thereby boost investor confidence (www.sec.gov.lk,2023).

The "Sri Lanka Accounting and Auditing Standard Act No. 15 of 1995," passed in 1995, greatly aided Sri Lanka's establishment of a culture of good governance. In compliance with this act, numerous actions have been made to enhance Sri Lanka's governance culture. The "Institute of Chartered Accountants of Sri Lanka (ICASL)" was given authority under this act to develop "Sri Lanka Accounting and Auditing Standards" as an example. The first official and formal corporate governance code published by ICASL, "The Code of Best Practices: Matters Relating to Financial Aspects of Corporate Governance," in December 1997 and this was based on the "Cadbury Code-1992 UK," the first English corporate governance code developed on the "Anglo-Saxon model." Despite the 'comply or explain' approach being adopted by the 'Cadbury Report on

Corporate Governance,' the ICASL code was a voluntary code. This can be considered the first corporate governance code in Sri Lanka (www.casrilanka.com, 2023).

"Handbook on Corporate Governance: Principles and Guidelines to best practices in Sri Lanka" was released in 2001 by the Institute of Chartered Secretaries and Administrators in Sri Lanka, another professional organization in the country. The Sri Lanka Branch of the Institute of Chartered Secretaries and Administrators (ICSA) was founded in 1953 as an Association of Sri Lankan Members of the Institute of Chartered Secretaries and Administrators (ICSA) of London. It was granted local status in 1985, and its name was changed to its current one in April 2008. (www.iccslk.org, 2023).

The "Best Practice on Audit Committees" was issued by the ICASL in 2002 which is another voluntary code on corporate governance and in the same year, CBSL also issued the "Code of Corporate Governance for Banks and Other Financial Institutions". The qualifications of directors, the role of the chairman and CEO, senior management, the company secretary, director training and familiarization, the structure of the board's committees, transparency, risk management practices, and prudential regulation and supervision are the 12 (twelve) corporate governance principles contained in this code. It is a voluntary code, and CBSL directed all banks to follow it in order to protect the financial system's integrity and stability (www.cbsl.gov.lk, 2023).

The "Code of Best Practices in Corporate Governance for Public Enterprises in Sri Lanka" was published by the "Department of Public Enterprises of the Ministry of Finance" in January 2003 with the goal of enhancing the corporate governance of public enterprises and statutory bodies. The Public Interest and Accountability to Stakeholders, Ownership Functions of Government and Relationship with Public Enterprise, Annual General Meeting on Enterprise Performance Strategy and Corporate Objectives, Boards for Effective Leadership and Oversight, Disclosures and Transparency, Performance-Related Incentives, etc. are just a few of the principles that are covered in detail in this code. The Code also addresses additional issues unique to the corporate governance of public enterprises, including the need for the government to exercise ownership and governance functions over public enterprises more effectively and the need for a professional board and management to have more operational independence from the government (Wickremasinghe, 2018).

The ICASL released the "Code of Best Practice on Corporate Governance" replacing the 1997 code and was based largely on Hampel Code 1998. This code contains the principles of corporate governance under two main headings: The Company and Institutional Shareholders. The section on 'The Company' provided

principles on corporate governance in relation to four main areas: directors; directors' remuneration; relations with shareholders; and accountability and audit. On the other hand, the section on 'Institutional Shareholders' provided principles on corporate governance in relation to institutional investors and other investors (www.casrilanka.com,2023).

In 2004, SEC issued another guideline on "Audit and Audit Committees" for listed companies (www.sec.gov.lk,2023).

1. In March 2007, the CSE included corporate governance in its listing rules. In the beginning, listed companies were instructed to publish a confirmation in the annual report for the financial year starting from 1 April 2007 indicating their compliance with the provisions of corporate governance rules provided in the listing rules (Section 7.10). If not, companies need to provide a written notice stating the reasons for non-compliance. In the second stage, it was mandated to comply with listing rules and need to publish a statement on compliance in the annual report commencing from April 1, 2008 (Manawaduge, 2012).

The CBSL issued two separate directions in December 2007 to "Licensed Commercial Banks (LCBs)" and "Licensed Specialized Banks (LSBs)" outlining the mandatory corporate governance criteria for banks in Sri Lanka (CBSL Annual Report, 2013a, 2013b). These two directions are mandatory for compliance and can be considered a milestone in the corporate governance reforms in Sri Lanka. These directions include basic corporate governance standards that are applicable to the banking industry in Sri Lanka. And another significant step toward a strong corporate governance culture was made in 2007 with the passage of the "Companies Act, No. 07 of 2007". That act included several provisions that support and build Sri Lanka's corporate governance culture (Menadue, 2012).

"ICASL" and "SEC" released the "Code of Best Practices of Corporate Governance" as a voluntary code of corporate governance in June 2008. The mutual responsibility of the single board for the performance of the company; the objectivity of the directors against the interests of the company; checks and balances; fairness of appointments and remuneration; and the effective rights of shareholders are some of the main topics covered by the code (Wickremesinghe,2018)

In order to improve the efficiency of the audit function in listed businesses, the "SEC" released a new guideline on the appointment of auditors in July 2008. A corporate governance directive (Corporate Governance Direction No. 3 of 2008) for Sri Lankan registered finance businesses was also released by the "Central Bank" in the same year with the objective of improving the corporate governance culture of registered finance companies in Sri Lanka. This direction has been amended in years 2008, 2011 and 2020. (Wickremasinghe, 2018).

A new corporate governance directive (Corporate Governance Direction No. 4 of 2009) was issued by the "Central Bank" to finance leasing businesses in 2009. It contains the directives for the responsibilities of the board, meetings of the board, criteria to assess the fitness and propriety of directors, the composition of the board, management functions delegated by the board, the Chairman and the Chief Executive Officer, board-appointed committees, related party transactions etc. This direction was issued by the CBSL aiming to streamline the corporate governance practices in finance companies post several failures in the financial sector. This direction was amended in 2013 and 2020 keeping with the changes in international standards. In the year 2012, CBSL issues another direction stating the criteria for the assessment of the fitness and propriety of the directors. (www.cbsl.gov.lk, 2023).

An updated "Code of Best Practice on Corporate Governance" was published in 2013 by "ICASL" and "SEC", jointly which improved the original code that was published in 2008. This code is mainly segregated into two parts; Company and Shareholders. "Reporting of internal controls, risk management and responsibilities of the board of directors and audit committees, requirements related to remuneration committee, the role of company secretary in relation to corporate governance of the company, communication with shareholders, and sustainability reporting" are some of the most significant changes made to the new code (www.casrilanka.lk, 2023).

CBSL issued two guidelines for LCBs and LSBs in 2015 to clarify the term "Key Management Personnel (KMPs)" mentioned in the 2007 corporate governance direction (www.cbsl.gov.lk, 2023).

With little changes, the "ICASL" published the fifth edition of the "Code of Best Practices of Corporate Governance" in the year 2017. Annual review of board composition against a predefined criterion, structured board meetings, defining and refining the role of the BOD, director's training, and authority to take expert advice, the introduction of related party transaction committee in line with the provisions of the CSE, a

requirement for "Environment, Society and Governance Reporting," etc. are some of the key vicissitudes suggested by this code. (www.casrilanka.lk, 2023).

The section pertaining to corporate governance in CSE listing rules have amended in 2018 to include the requirement of an audit committee (Rule 7.10.6 (a). Accordingly, a listed entity must comply with the audit committee requirements stipulated in the directions with regard to composition, function, and disclosures in the annual report of the audit committee (www.cse.lk,2023).

Banking act directions nos. 11 and 12 of 2007 on corporate governance for licensed banks in Sri Lanka were modified in 2019 to include section 3 (iii) which stipulates the appointment of directors to licensed banks (www.cbsl.gov.lk,2023).

In 2019, ICASL published a “Guide to Corporate Governance in Small and Medium Enterprises” in order to develop sound corporate governance practices and thereby evolve the SME industry in Sri Lanka. This guide specifically highlights the application of corporate governance in SMEs, strategy, structures, and responsibilities as SMEs are considered as aspiring corporates in a country (www.casrilanka.lk, 2023).

CBSL issued another direction, the finance business Act Direction No. 05 of 2021 on corporate governance applicable to finance companies during the covid 19 pandemic to strengthen the corporate governance practices of the finance companies (www.cbsl.gov.lk,2023).

These numerous regulations issued by various regulatory authorities exhibit their interest in maintaining good governance culture in their respective sectors. However, it is also evident there was a lack of coordination between these institutions when codifying corporate governance rules in Sri Lanka (Wickremasinghe,2018).

Table 1.0- Summary of “Corporate Governance Codes” and “Rules” in Sri Lanka

Year	Issued Institution	Name of the Code	Content Summary
1997	Institute of Chartered Accountants of Sri Lanka	Code on Best Practices on Matters Relating to Financial Aspects of Corporate Governance (Blue Print of the Cadbury Code 1992)	Structure and responsibilities of the BOD. Rights and responsibilities of the Shareholders. Role of auditors
2001	Institute of Chartered Secretaries and Administrators in Sri Lanka” (Now known as Institute of Chartered Corporate Secretaries of Sri Lanka)	Hand Book on Corporate Governance: Principles and Guidelines to Best Practice in Sri Lanka	Principles and Guidelines to Best Practice in Sri Lanka
2002	Institute of Chartered Accountants of Sri Lanka	Code of Best Practices on Audit Committee	Scope and functions of the audit committee of listed companies.
2002	Central Bank of Sri Lanka	Voluntary Code on Corporate Governance	This code consists of 12 basic principles of corporate governance related to board; namely, the qualification of directors, chairman and CEO, the role of CEO and senior management, company secretary, directors’ training/familiarization, committee structure for board, transparency, risk management systems and prudential

			regulation and supervision.
2003	Institute of Chartered Accountants of Sri Lanka	Code of Best Practice on Corporate Governance (Replaced 1997 Code and based largely on Hampel Code (1998))	<p>Principles on corporate governance under two main headings: The Company and Institutional Shareholders.</p> <p>The section on ‘The Company’ provided principles on corporate governance in relation to four main areas: directors; directors’ remuneration; relations with shareholders; and accountability and audit. On the other hand, the section on ‘Institutional Shareholders’ provided principles on corporate governance in relation to institutional investors and other investors.</p>
2003	Department of Public Enterprises of the Ministry of Finance	Code of Best Practices in Corporate Governance for Public Enterprises in Sri Lanka	<p>The Public Interest and Accountability to Stakeholders</p> <p>Ownership Functions of the Government and Its Relationship with the Public Enterprise</p> <p>The Annual General Meeting on Enterprise Performance, Strategy and Corporate Objectives</p>

			Boards for Effective Leadership and Oversight Disclosures and Transparency Performance-Related Incentives
2004	Securities and Exchange Commission	Guideline for Listed Companies on Audit and Audit Committees	
2007	Colombo Stock Exchange	Listing Rules 2007 Section 6	Non-Executive Directors Independent Directors Disclosures relating to directors Remuneration Committee & Audit Committee
2007	Central Bank of Sri Lanka	Banking Act Direction No. 11 of 2007- Corporate Governance for Licensed Commercial Banks in Sri Lanka	The Responsibilities of the Board The Board's composition Criteria to assess the Fitness and Propriety of Directors Management functions delegated by the Board The Chairman and the Chief Executive Officer Board appointed Committees

			Related party transactions
2007	Central Bank of Sri Lanka	Direction No. 12 of 2007 – Corporate Governance for Licensed Specialized Banks in Sri Lanka	<p>The Responsibilities of the Board</p> <p>The Board's composition</p> <p>Criteria to assess the Fitness and Propriety of Directors</p> <p>Management functions delegated by the Board</p> <p>The Chairman and the Chief Executive Officer</p> <p>Board appointed Committees</p> <p>Related party transactions</p>
2008	Institute of Chartered Accountants of Sri Lanka and Securities and Exchange Commission of Sri Lanka jointly.	Code of Best Practice on Corporate Governance	<p>A single board collectively responsible for the success of the company</p> <p>A separate Chief Executive and Chairman</p> <p>A balance of Executive and Independent Non-Executive Directors</p> <p>Strong, independent Audit and Remuneration Committees</p> <p>Annual evaluation by the Board</p>

			<p>of its own performance</p> <p>Emphasis of objectivity of directors in the interest of the company</p> <p>Transparency on appointment and remuneration</p> <p>Effective rights of shareholders</p>
2008	Central Bank of Sri Lanka	<p>1. Corporate Governance Direction No. 5 of 2008- Amendments to Directions on Corporate Governance for Licensed Commercial Banks in Sri Lanka.</p> <p>2. Corporate Governance Direction No. 7 of 2008 Amendments to Directions on Corporate Governance</p>	<p>The Banking Act Direction No. 1 of 2008 dated April 23, 2008 described as “Provisions regarding executive directors and transitional provisions for founding directors, incumbent chairmen and executive directors”, was revoked. And following sections were replaced in the 2007 direction.</p> <p>3(2)(ii) (B)</p> <p>3(3)(i)(A) and 3(3)(i)(B)</p> <p>3(3)(ii)</p> <p>3(9)(v)</p> <p>Replaced the Direction No. 5 of the Banking Act, Direction No. 5 of 2008</p>

		for Licensed Commercial Banks in Sri Lanka.	
2008	Central Bank of Sri Lanka	<p>1. Banking Act Direction No. 6 of 2008 amendments to Directions on Corporate Governance for Licensed Specialized Banks in Sri Lanka.</p> <p>2. Banking Act Direction No. 8 of 2008 amendments to Directions on Corporate Governance for Licensed Specialized Banks in Sri Lanka.</p>	Amendments to Banking Act Direction No. 12 of 2007- Corporate Governance for Licensed Specialized Banks in Sri Lanka
2008	Central Bank of Sri Lanka	Finance Companies Corporate Governance Direction No. 3 of 2008.	<p>The Responsibilities of the Board</p> <p>Meetings of the board</p> <p>Composition of the board</p> <p>Criteria to assess the Fitness and Propriety of Directors</p> <p>Delegations of functions</p>

			<p>The Chairman and the Chief Executive Officer</p> <p>Board appointed Committees</p> <p>Related party transactions</p>
2008	Central Bank of Sri Lanka	Finance Companies Corporate Governance (Amendment) Direction No. 4 of 2008	<p>Amended the previous direction issued same year (“Finance Companies Corporate Governance Direction No. 3 of 2008”)</p>
2008	Securities and Exchange Commission	Guidelines for Appointment of Auditors of Listed Companies	<p>Qualification & Appointment of Auditors</p> <p>Rotation of Partners</p> <p>Re-appointment of Engagement Partner</p> <p>Independence of Auditors</p> <p>Financial Reporting</p>
2009	Central Bank of Sri Lanka	Finance Leasing (Corporate Governance) Direction No. 4 of 2009	<p>The Responsibilities of the Board</p> <p>Meetings of the board</p> <p>Composition of the board</p> <p>Criteria to assess the Fitness and Propriety of Directors</p> <p>Management function delegated</p>

			<p>by the board</p> <p>The Chairman and the Chief Executive Officer</p> <p>Board appointed Committees</p> <p>Related party transactions</p>
2009	Colombo Stock Exchange	Listing Rules 2009 (Section 7.10)	Corporate governance requirements related to compliance, non-executive directors, independent directors, disclosure related to directors, criteria for defining independence, the remuneration committee, and the audit committee.
2013	Institute of Chartered Accountants of Sri Lanka” and “Securities and Exchange Commission of Sri Lanka” jointly.	Code of Best Practice on Corporate Governance”	The key changes introduced to the new code include “reporting of internal controls, risk management and responsibilities of board of directors and audit committees, requirements related to remuneration committee, the role of company secretary in relation to the corporate governance of the company, communication with shareholders and sustainability reporting.
2013	Central Bank of Sri Lanka	Banking Act direction No. 3 of 2013	Replace Direction No 3(3)(ii) of the Banking Act, Direction No.

		Amendments to directions on Corporate Governance issued to Licensed Commercial Banks in Sri Lanka	11 of 2007, dated 26 December 2007.
2013	Central Bank of Sri Lanka	Banking Act Direction No. 04 of 2013– Amendments to Direction on Corporate Governance Issued to Licensed Specialized Banks in Sri Lanka	Amendment to “Banking Act Direction No. 12 of 2007 Corporate Governance for Licensed Specialized Banks in Sri Lanka.
2013	Central Bank of Sri Lanka”	Finance Companies (Corporate Governance Amendment) Direction No. 6 of 2013	Amendment to “Finance Companies Corporate Governance Direction No. 3 of 2008”
2013	Central Bank of Sri Lanka	Finance Leasing (Corporate Governance- Amendment) Direction No. 1 of 2013	Finance Leasing (Corporate Governance) Direction No. 4 of 2009”
2015	Central Bank of Sri Lanka	Key Management Personnel in Banking Act Direction on Corporate Governance	Clarifying the term “Key Management Personal (KMPs)” mentioned in the 2007 corporate governance direction.
2017	Institute of Chartered Accountants of Sri Lanka	Code of Best Practices of Corporate Governance (5 th edition)	Annual review of board composition against a predefined criterion, structured board meetings, define and

			refine role of the BOD, Director's training, and authority to take expert advice, Introduction of related party transaction committee in line with the provisions of the CSE, a requirement for 'Environment, Society and Governance Reporting etc.
2018	Colombo Stock Exchange	Amendments made to the CSE Listing Rules in the Year 2018	Rule 7.10.6 (a) - Composition and Role of the Audit Committee
2019	Central Bank of Sri Lanka	Banking Act No. 9 of 2019 on Corporate Governance for Licensed Banks in Sri Lanka	<p>Amendment to the "Banking Act No. 11 and 12 of 2007 on Corporate Governance for Licensed Banks in Sri Lanka"</p> <p>Insert 3 (3) iii to the original direction.</p> <p>(A Director or a Chief Executive Officer of a licensed bank operating in Sri Lanka shall not be appointed as a Director or a Chief Executive Officer of another licensed bank operating in Sri Lanka before the expiry of a period of 6 months from the date of cessation of his/her office at the licensed bank in Sri Lanka. Any variation thereto in exceptional situations such as where</p>

			<p>expertise of retiring bankers maybe required when reconstituting Boards of licensed banks which need restructuring, shall be subject to the prior approval of the Monetary Board. In this regard, licensed banks shall ensure to adhere to the requirement of the cooling-off period when appointing Directors or Chief Executive Officer. If a Director is appointed to the licensed bank by an appointing authority violating these Directions, the licensed bank shall take steps to prevent such appointee from exercising any powers or enjoying any privileges or benefits).</p>
2019	Institute of Chartered Accountants of Sri Lanka	Guide to Corporate Governance in Small and Medium Enterprises	<p>Application of Corporate Governance in SMEs</p> <p>Strategy</p> <p>Structure and responsibility of the board</p>
2021	Central Bank of Sri Lanka	Finance Business Act Direction No. 5 of 2021	<p>Boards overall responsibilities</p> <p>Governance Framework</p> <p>Composition of the board</p> <p>Assessment of fitness and propriety criteria</p> <p>Appointment and Resignation</p>

			of directors and senior management The Chairperson and the CEO Meetings of the board Company Secretary Delegations of functions by the board Board sub committees Internal controls Related Party Transactions Group Governance Corporate Culture Conflicts of interest Disclosures
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Corporate Governance Directions Applicable to the Banking Industry in Sri Lanka

1. CBSL Directions for LCBs and LSBs

The Central Bank of Sri Lanka has issued two directions on corporate governance that are applicable to the banking industry.

1. Banking Act Direction No. 11 of 2007 on Corporate Governance
2. Banking Act Direction No. 12 of 2007 on Corporate Governance

As mentioned above, these directions were amended from time to time to be in line with the market and economic conditions. These two directions mainly focused on the “responsibilities of the board, the board's composition, criteria to assess the fitness and propriety of directors, management functions delegated by the board, the Chairman and the Chief Executive Officer, the board-appointed committees, related party transactions and disclosures” (www.cbsl.gov.lk,2023).

The compliance with the said directions was ascertained by the CBSL officers by conducting onsite audits and off-site audits. In addition, the banks are required to provide a statement on the level of compliance with the said directions in their respective annual reports. (www.cbsl.gov.lk,2023).

2. Listing Rules on Corporate Governance

The listing rules are mandatory for the companies listed on CSE. Corporate governance is considered a prerequisite under the Colombo Stock Exchange's current listing regulations, which were last updated on 14th February 2022. Every applicant for listing securities must adhere to listing rules, which are expressly stated in the listing regulations. In addition to the firms' statutory requirements, these listing standards impose new obligations that are both complimentary and supplementary. Corporate governance is expressly included in Section 7.10 of the listing rules. It outlines the rules for corporate governance in relation to compliance, independent directors, non-executive directors, disclosure related to directors, criteria for defining independence, the remuneration committee, and the audit committee and also the enforcement procedure for non-compliance with corporate governance requirements (www.cse.lk, 2023).

3. Code of Best Practice on Corporate Governance – 2017

This is the most recent corporate governance code that the ICASL has published. Despite being a voluntary code of corporate governance, the majority of corporate bodies adhere to it. In this code, corporate governance is covered from two angles.. i.e., the Company perspective and the shareholder perspective. Corporate governance principles related to directors, remuneration of directors, relations with shareholders, accountability and auditing are discussed from the company's perspective. In contrast, corporate governance issues pertaining to institutional investors, other investors, the Internet of things and cyber security, as well as environment, society, and governance (ESG) reporting are considered from the viewpoint of the shareholders. It appears that the Code of Best Practice on Corporate Governance is a thorough code that takes into account all of the corporate governance's fundamental features (www.casrilanka.com,2023).

Legal Framework of Corporate Governance Applicable to the banking industry in Sri Lanka

This section discusses some of the key legislative enactments that are related to the corporate governance structure of Sri Lankan banks. While some legislations contain notions related to corporate governance expressly, other laws act as the framework for developing such concepts through rules, regulations, guidelines, and directives (Wickremasinghe, 2018).

1. Monetary Law Act No. 58 of 1949

The Monetary Law Act is one of the key statutes in Sri Lanka which had gained more importance due to the prevailing financial crisis. It was incorporated in 1949 with the view of establishing a monetary system in the Country. The CBSL has been established under Section 5 (Chapter II) and the Monetary Unit was established under Section 1 (Chapter I) of this act. The Monetary Board has the authority to create rules and regulations that are required with regard to any issues impacting the Central Bank's powers, responsibilities, and obligations under Section 10 (c) of the Monetary Law Act. Maintaining the stability of the nation's financial system in accordance with section 5 of the Act is one of the Central Bank's primary objectives. The Monetary Board uses the power granted to it by Section 10(c) read in conjunction with Section 5 to create corporate governance standards for banks because corporate governance improves banking stability, which in turn improves the stability of the country's financial system (www.cbsl.gov.lk, 2023). Sri Lanka is currently in the process of amending the Monetary Law Act to grant more independence to CBSL to operate flexible policy and implement both monetary and exchange rate policy (www.economynext.com, 2023).

2. Banking Act No. 30 of 1988

The banks in Sri Lanka are established and regulated under the banking act. The banking act was amended in 1990, 1995, 2005 and 2006. The guidelines for corporate governance are given to LCBs and LSBs by the Monetary Board of the CBSL under the banking act section 46 (1) and 76 (j) (1) respectively. Schedule II of the Banking Act provides the list of activities that banks are permitted to carry out by a LCB and Schedule IV provides for the list of activities that are permitted to carry out by a LSB. (www.cbsl.gov.lk, 2023). According to the Deputy Governor Ms T M J Y P Fernando, CBSL is amending the banking act as a part of the IMF bailout negotiations and expects to finalize it within the year 2023 (www.dailynews.lk, 2022).

3. Sri Lanka Accounting and Auditing Standards Act No. 15 of 1995

The main regulating law of Sri Lanka's accounting system is the Accounting and Auditing Standards Act No. 15 of 1995. Enforcing this law is the responsibility of the Sri Lankan Accounting and Auditing Standards Monitoring Board (SLAASMB). All Specified Business Entities (SBEs), including banks, are required under the act to compile and present financial statements in accordance with its requirements (www.casrilanka.com,2023).

This Act has a few notable features. According to sections 2 and 3 of this act, the Institute of Chartered Accountants of Sri Lanka (ICASL) is empowered to implement Sri Lankan accounting and auditing standards. Further, the Sri Lanka Accounting Standard Monitoring Board, a board which monitors compliance with the act by the stakeholders was established by section 11 of the act (www.casrilanka.com,2023).

4. Companies Act No. 7 of 2007

The company law of Sri Lanka runs back to the British era. The Joint Stock Company Ordinance No 4 of 1861 was the first piece of legislation developed especially for Sri Lanka. Then there were many other statutes such as Companies Ordinance No. 15 of 1938, Companies Act No. 17 of 1982 etc. In 2007, all these statutes were repealed and the Companies Act No. 7 of 2007 was enacted which consolidates all the laws applicable to the companies in Sri Lanka. This is a considerably lengthy and comprehensive statute (Wickremasinghe,2018).

The Companies Act contains a number of provisions that are designed to enhance and facilitate corporate governance. The fundamental obligations of the directors to the company are spelt forth in detail (www.drc.gov.com, 2023).

There are also other laws that support the establishment of Sri Lanka's corporate governance structure. The Finance Companies Act, No. 78 of 1988, and the Finance Leasing Act, No. 56 of 2000, are two examples of such laws. These Acts form the basis for developing corporate governance in particular sectors like finance and leasing (Wickremasinghe,2018).

Conclusion

In Sri Lanka, corporate governance has a long history that dates back to the reign of the ancient monarchs. However, the institutional and framework developments pertaining to corporate governance are far more recent. As depicted above, there are various rules, regulations, and voluntary and non-voluntary codes that codified the corporate governance standards in Sri Lanka. These Rules and Codes are backed by several key statutes such as the Banking Act No.30 of 1988 Sri Lanka, Monetary Law Act No. 58 of 1949 of Sri Lanka, Companies Act No. 7 of 2007 of Sri Lanka, and Sri Lanka Accounting and Auditing Standards Act No. 15 of 1995 etc. The corporate governance regime appears adequate considering the economic background and the country's market size. However, one may have to refer to several statutes to get an understanding of the corporate governance structure in the financial industry in Sri Lanka. This article provides a gateway for that requirement. However, a time had come to the codification of these rules and regulations applicable to corporate governance as it will be more convenient and practical for the stakeholders to refer to a single document rather than referring to various documents. Moreover, it will improve the level of compliance with corporate governance standards for obvious reasons.

There is very little research work available as of date on the effectiveness of those regulations and codes. Therefore, there is more scope for research in this area.

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