

The Hongkong and Shanghai Banking Corporation  
Limited – Sri Lanka Branch

# Disclosures on Corporate Governance 2020



## ***Independent Assurance Report***

### ***To the Branch Management of the Hongkong & Shanghai Banking Corporation- Sri Lanka Branch***

1. We were engaged by the Branch Management of the Hongkong & Shanghai Banking Corporation- Sri Lanka Branch (“the Branch”) to provide assurance on the Branch Management Statement on Internal Control (“the Statement”) for the year ended 31 December 2020.

#### *The Branch Management’s responsibility*

2. The Branch is responsible for the preparation and presentation of the Statement in accordance with the “Guidance for Directors of Banks on the Directors’ Statement on Internal Control” issued in compliance with the section 3(8)(ii)(b) of the Banking Act Direction No. 11 of 2007, by the Institute of Chartered Accountants of Sri Lanka.

#### *Our responsibilities and compliance with SLSAE 3050*

3. Our responsibility is to issue a report to the Branch on the Statement based on the work performed. We conducted our engagement in accordance with Sri Lanka Standard on Assurance Engagements SLSAE 3050 – Assurance Report for Banks on Directors’ Statement on Internal Control issued by the Institute of Chartered Accountants of Sri Lanka.

#### *Summary of work performed*

4. Our engagement has been conducted to assess whether the Statement is both supported by the documentation prepared by or for the Branch and appropriately reflects the process the Branch has adopted in reviewing the system of internal control for the Branch.

5. To achieve this objective, appropriate evidence had been obtained by performing the following procedures:

- (a) Enquired from the Branch and obtained an understanding of the process defined by the management for their review of the design and effectiveness of internal control and compared their understanding to the statement made by the Branch.
- (b) Reviewed the documentation prepared by the Branch to support their Statement.
- (c) Related the Statement made by the Branch to the auditor’s knowledge of the Branch obtained during the audit of the financial statements.
- (d) Reviewed the minutes of the meetings of the Executive Committee and of relevant other Management Committees of the Branch.

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- (e) Considered whether the Management Statement on Internal Control covers the year under review and that adequate processes are in place to identify any significant matters arising.
- (f) Obtained written representations from the Branch on matters material to the Statement on Internal Control when other sufficient appropriate audit evidence cannot reasonably be expected to exist.
- (g) Discussed with the Branch whether steps have been taken by them to determine what process it has applied to deal with material internal control aspects of any significant problems.
- (h) Obtained an understanding from the Branch as to whether there is an ongoing process for identifying, evaluating and managing the significant risks faced by the bank, whether it has been in place for the year under review, whether it is regularly reviewed and whether the explanations are consistent with auditor's understanding.

6. SLSAE 3050 does not require us to consider whether the Statement covers all risks and controls, or to form an opinion on the effectiveness of the Branch's risk and control procedures. SLSAE 3050 also does not require us to consider whether the processes described to deal with material internal control aspects of any significant problems disclosed in the financial statements will, in fact, remedy the problems.

Our conclusion

7. Based on the procedures performed, nothing has come to our attention that causes us to believe that the Statement is inconsistent with our understanding of the process the management has adopted in the review of the design and effectiveness of internal control of the Branch.

[Signed]

**CHARTERED ACCOUNTANTS  
COLOMBO**  
25 May 2021



**THE HONGKONG AND SHANGHAI BANKING CORPORATION LIMITED**  
**SRI LANKA BRANCH**  
**STATEMENT OF COMPLIANCE**

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The Hongkong & Shanghai Banking Corporation Limited – Sri Lanka Branch ('HSBC Sri Lanka') is registered in Sri Lanka as a branch of The Hongkong and Shanghai Banking Corporation Limited ('the Company'), a company incorporated in Hong Kong. HSBC Holdings plc, a company incorporated in England, is the ultimate holding company.

HSBC Sri Lanka has effective processes in place to ensure compliance with all applicable laws and regulations pertaining to the banking industry in Sri Lanka, and the Central Bank of Sri Lanka directions and guidelines. Additionally, the Bank is bound to comply with the applicable directions of the Company. The Banking Act Direction No. 11 of 2007 and its amendments ("the Direction") on Corporate Governance for Licensed Commercial Banks in Sri Lanka, issued by the Monetary Board of the Central Bank of Sri Lanka under section 46 (1) of the Banking Act No. 30 of 1988 provides the mandatory requirements set out in section 3 of the said Direction that should be complied with by Licensed Commercial Banks. All branches of foreign banks are requested to adhere to sections 3 (8) and 3 (9) of the said Direction and HSBC Sri Lanka complies with the same on Corporate Governance.

The Company has adopted an integrated operational risk and internal control management framework, referred to as the Three Lines of Defence model. The model ensures it achieves its commercial aims while meeting regulatory and legal requirements and its responsibilities to shareholders, customers and staff.

**The First Line of Defence**, comprising of a majority of employees, identifies the risks and ensures that the right controls are in place to prevent, manage, and reduce the risks including the delivery of fair conduct outcomes

The Risk Owners in the Lines of Businesses are accountable for setting risk appetite, identifying, owning, and managing non-financial risks for their Business in line with appetite, i.e. within the limits set out by the HSBC Group. The Control Owners, who may sit within a Lines of Business or Function within HSBC, monitor, assess and manage the processes, activities, or systems to ensure that they are operating effectively. They work with the Risk Owners to understand and manage the risks. The Chief Control Officers (CCO), who may sit within a Lines of Business or Functions, drive effective governance and management of non-financial risks for their organization area. They work closely with Risk Owners and Control Owners to ensure operational risk management activities are effectively executed.

**The Second Line of Defence** consisting of "Chief Risk Officers", "Risk Stewards" and "Operational Risk" functions, provide review and challenge of First Line of Defence activities to help ensure risk management decisions and actions are appropriate, within risk appetite and support the delivery of conduct outcomes. The Second Line of Defence is independent of the day to day commercial risk-taking activities undertaken by the First Line of Defence. The Chief Risk Officers oversee the risk management for areas within their remit. The Risk Stewards, sitting within the Functions, perform the specialist role in the review and challenge of, and subject matter expert for, the First line of Defence activities for a given risk type. The Operational Risk function provides advice and guidance on the use of the Risk Management Framework. They also challenge the effectiveness of the framework in use both in the first and second lines of defence.

**The Third Line of Defence** is Internal Audit which independently assures that the HSBC is managing its non-financial risks effectively.

The Compliance function is a Second line of defence function, responsible for reviewing and challenging the activities of the First Line of Defence to ensure that they effectively manage as Risk Owners the risks inherent in or arising from the conduct of their activities and for which they are

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responsible. Compliance function is a Risk Steward for a number of non-financial risks in accordance with HSBC Group's risk framework including Financial Crime and Regulatory Compliance Risks.

Stewardship of Financial Crime Risks is focused on:

Countering financial crime by identifying, analysing, and investigating Financial Crime risk to support informed risk management and effective information sharing with internal and external stakeholders grounded in advanced analytics and technology.

Working with the Lines of Business to set policy and provide effective oversight of the operational effectiveness of critical policies and systems covering financial crime that ensure that the country exposure to financial crime and related reputational risk is managed, in a commercially sensitive and practical manner.

Articulating country risk appetite and policies with respect to money laundering, sanctions, internal and external fraud, tax evasion, terrorist financing, bribery and corruption.

Ensuring timely reporting and disclosure of relevant information both to regulators and within the Group in relation to financial crime matters.

Stewardship of Regulatory Compliance Risks is focused on:

Understanding the regulatory landscape and working with the Lines of Business to help them identify and manage their regulatory compliance risks. Providing independent and objective oversight and challenge, and promote a compliance-orientated culture, supporting the business in delivering fair outcomes for customers and achieving HSBC's strategic objectives.

Setting the policies and standards which cover HSBC's regulatory requirements, and support the management of Conduct and Reputational Risk issues.

Understanding the regulatory change agenda and ensure that the businesses understand the implications.

Further the Regulatory Conduct team will:

- Oversee delivery of key compliance risk related regulatory commitments
- Oversee and support continued improvement and embedding of the Group's Whistleblowing arrangements and Conduct framework.

2021 will see the Bank take action to adapt to a continually changing world. Compliance will play a critical role in supporting, challenging and advising the Lines of Business. Compliance will respond to industry and HSBC Group strategic changes by evolving as a function for the future based on four key principles:

- Technology and Advanced Capabilities
- Simplification
- Risk Management
- Navigating the Regulatory Landscape

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In addition to the above, the Compliance Assurance function is responsible for carrying out monitoring activities to provide a reasonable assurance to the Lines of Business that their First Line of Defence is sound and sufficient. This is being established through two main activities:

- By testing the adequacy of existing FC and RC controls in both the First Line and Second Line of Defence
- By identifying any gaps in the control environment and advising both the Lines of Defence to develop or maintain controls to mitigate any potential risks.

[Signed]

**Matthew K Lobner**

Head of International, Asia Pacific

Head of Strategy & Planning, Asia Pacific

[Signed]

**Mark G Prothero**

Chief Executive Officer, HSBC Sri Lanka and Maldives

Date: 20 May 2021

**THE HONGKONG AND SHANGHAI BANKING CORPORATION LIMITED**  
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**HEAD OFFICE STATEMENT ON CONTROLS**

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**RESPONSIBILITY**

The Hong Kong & Shanghai Banking Corporation Limited – Sri Lanka Branch ('HSBC Sri Lanka') is registered in Sri Lanka as a branch of The Hong Kong and Shanghai Banking Corporation Limited ('the Company'), a company incorporated in Hong Kong, and as such follows all policies and procedures laid out by the Company. HSBC Holdings plc, a company incorporated in England, is the ultimate holding company.

In line with the Banking Act Direction No. 11 of 2007, Section 3 (8) (ii) (b), and the subsequent circular 02/17/550/002/002 dated 3rd January 2011, the Head of the Office supervising HSBC Sri Lanka, namely HSBC International, presents this Report on Internal Control.

HSBC International, together with the regional teams of Global Businesses and Global Functions ("collectively the "Head Office"), are responsible for overseeing the implementation of the system of internal controls at HSBC Sri Lanka ('the Bank'). This system is designed to manage the Bank's key areas of risk within an acceptable risk profile, rather than to eliminate the risk of failure to achieve the policies and business objectives of the Bank. Accordingly, the system of internal controls can only provide reasonable but not absolute assurance against material misstatement of management and financial information and records or against financial losses or fraud.

HSBC Group has established an ongoing process for identifying, evaluating and managing the significant risks faced by the Bank and this process includes enhancing the system of internal controls as and when there are changes to the business environment or regulatory guidelines. HSBC Sri Lanka has regularly reviewed the process and further considered the Guidance for Directors of Banks on the Directors' Statement on Internal Control issued by the Institute of Chartered Accountants of Sri Lanka taking into account principles for the assessment of internal control systems as given in that guidance.

The Head Office is of the view that the system of internal controls in place is sound and adequate to provide reasonable assurance regarding the reliability of financial reporting, and the preparation of Financial Statements for external purposes has been done in accordance with Sri Lanka Accounting Standards and regulatory requirements of the Central Bank of Sri Lanka.

The Chief Executive Officer ("CEO") and the Executive Committee ("EXCO") of HSBC Sri Lanka, together assist the Head Office in the implementation of policies and procedures on risk and control by identifying and assessing the risks faced, and in the design, operation and monitoring of suitable internal controls to mitigate and control these risks.

**KEY PROCESSES ADOPTED AND APPLIED IN REVIEWING THE DESIGN AND EFFECTIVENESS OF THE INTERNAL CONTROL SYSTEM ON FINANCIAL REPORTING**

The key processes that have been established in reviewing the adequacy and integrity of the system of internal controls with respect to financial reporting include the following:

Various committees have been established to ensure the effectiveness of the Bank's daily operations and that the Bank's operations are in accordance with the corporate objectives, strategies and the annual operating plan as well as the policies and business directions that have been approved.

All employees are responsible for identifying and managing risk within the scope of their role as part of the three lines of defence model, which is an activity-based model to delineate management accountabilities and responsibilities for risk management and the control environment. The second line of defence sets the policy and guidelines for managing specific risk areas, provides advice and guidance in relation to the risk, and challenges the first line of defence (the risk owners) on effective risk management.

The primary role of the Global Internal Audit function as the third line of defence is to help the Board and management protect the assets, reputation and sustainability of the Group. Global Internal Audit does this by

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providing independent and objective assurance on the design and operating effectiveness of the Group's governance, risk management and control framework and processes, prioritising the greatest areas of risk.

Responsibilities of Group Audit Committee ('GAC') include:

- monitoring and assessing the integrity of the financial statements, formal announcements and regulatory information in relation to the Group's financial performance, as well as significant accounting judgements;
- reviewing the effectiveness of, and ensuring that management has appropriate internal controls over, financial reporting;
- reviewing and monitoring the relationship with the external auditor and oversees its appointment, tenure, rotation, remuneration, independence and engagement for non-audit services; and
- overseeing the work of Global Internal Audit and monitoring and assessing the effectiveness, performance, resourcing, independence and standing of the function.

Local Senior Management ensures compliance with policies and procedures and where there has been a breakdown in internal controls, or breach of authority, the CEO is advised in a timely manner. Additionally, such issues are escalated and tabled at the monthly Risk Management Meeting ("RMM"). Where the CEO deems the issue material, it is reported up the functional and management lines to Regional Functions and GBL INA.

Global Internal Audit – Sri Lanka & Maldives is primarily responsible to:

- Provide independent and objective assurance as to whether the design and operational effectiveness of the Group's framework of risk management, control and governance processes, as designed and represented by management, is adequate.
- Implementing the approved Audit Plan, including any regulatory or other special tasks or projects requested by regulators and local Risk Committees;
- Implement risk based Audit coverage through a combination of business and functional governance audits, process and control audits, risk management framework audits, themed audits, and project audits. In addition, Audit may carry out Regulatory audits, investigations and special reviews.

The comments made by the external auditors and the internal audit department in connection with internal control system in the financial year to 31st December 2019 were reviewed during the year and appropriate steps have been taken to rectify them. The recommendations made by the external auditors and the internal audit department in the financial year to 31st December 2020 in connection with the internal control system have already been dealt with and in some instances are in the process of being actioned upon. The Management is of the opinion that these recommendations are intended to further improve the internal control system and they do not in any way detract from the conclusion that the financial reporting system is reliable to provide reasonable assurance that the financial statements for external use are true and fair and comply with Sri Lanka Accounting Standards (SLFRS & LKAS) and the regulatory requirements of the Central Bank of Sri Lanka (CBSL).

**CONFIRMATION**

Based on the above, the Regional Finance in Head Office confirms that the financial reporting system of the Bank has been designed to provide reasonable assurance regarding the reliability of financial reporting and that the preparation of Financial Statements for external purposes has been done in accordance with Sri Lanka Accounting Standards and regulatory requirements of the Central Bank of Sri Lanka.

**REVIEW OF THE STATEMENT BY EXTERNAL AUDITORS**

The External Auditors have reviewed the above Head Office Statement on Internal Control of the Bank for the year ended 31st December 2020 and reported to the Bank that nothing has come to their attention that causes them to believe that the statement is inconsistent with their understanding of the process adopted by



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the Management in the review of the design and effectiveness of the internal control system over financial reporting of the Bank.

By order of HSBC International,  
The signatories for the bank

[Signed]

**Matthew K Lobner**

Head of International, Asia Pacific

Head of Strategy & Planning, Asia Pacific

[Signed]

**Mark G Prothero**

Chief Executive Officer Sri Lanka and Maldives

Date: 20 May 2021

**THE HONGKONG AND SHANGHAI BANKING CORPORATION LIMITED**  
**SRI LANKA BRANCH**  
**DISCLOSURES ON CORPORATE GOVERNANCE**

**1 DETAILS OF ACCOMODATION GRANTED AS AT 31 DECEMBER 2020**

**1.1 Total accommodation granted to each category of related parties (in LKR ‘000)**

Bank’s subsidiary companies	N/A
Bank’s associate companies	N/A
Directors of the bank	N/A
Bank’s key management personnel	462,490
A close relation of any of the bank’s directors or key management personnel	18,595
A shareholder owning a material interest in the bank	N/A
A concern in which any of the bank’s directors or a close relation of any of the bank’s directors or any of its material shareholders has a substantial interest	N/A

**1.2 Total accommodation granted to each category of related parties as a percentage of the bank’s regulatory capital**

Bank’s subsidiary companies	N/A
Bank’s associate companies	N/A
Directors of the bank	N/A
Bank’s key management personnel	0.710%
A close relation of any of the bank’s directors or key management personnel	0.029%
A shareholder owning a material interest in the bank	N/A
A concern in which any of the bank’s directors or a close relation of any of the bank’s directors or any of its material shareholders has a substantial interest	N/A

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**DISCLOSURES ON CORPORATE GOVERNANCE**

**2 TRANSACTIONS OF THE BANK WITH ITS KEY MANAGEMENT PERSONNEL**

	LKR '000
Aggregate remuneration paid for the year ended 31 December 2020	456,987
Total accommodation granted as at 31 December 2020	462,490
Total deposits as at 31 December 2020	124,358
Total investments made as at 31 December 2020	NIL

**3 STATEMENT OF REGULATORY AND SUPERVISORY CONCERNS**

We confirm that to the best of our knowledge that The Hong Kong and Shanghai Banking Corporation Limited Sri Lanka have not encountered any supervisory concerns on lapses in bank's risk management, or non-compliance with these Directions that have been pointed out by the Director of Bank Supervision, if so directed by the Monetary Board to be disclosed to the public.

[Signed]

**Mark G Prothero**

Chief Executive Officer

HSBC Sri Lanka and Maldives

[Signed]

**Angelo Pillai**

Chief Financial Officer

HSBC Sri Lanka and Maldives

Date: 25 May 2021