

## FINANCIAL REPORTS

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1. The Directors present herewith the audited consolidated financial statements of Sri Lanka Telecom PLC ('SLTPLC' or 'the Company') and its subsidiaries ('the Group') for the year ended 31 December 2007.

### 2. FORMATION

Sri Lanka Telecom (SLT) was formed by an Incorporation Order made under Section 2 of the State Industrial Corporations Act No. 49 of 1957 and published in the Extraordinary Gazette No. 596/11 of 6 February 1990. Subsequently, in terms of an Order made by the Minister of Posts and Telecommunications ('the Minister') on 24 July 1991 under Section 23 of the Sri Lanka Telecommunications Act No. 25 of 1991 and published in the Gazette No. 675 of 9 August 1991, all properties, rights and liabilities (other than those excluded by the agreement entered into between the Minister and SLT as per sub-section 2 of Section 23 of the Sri Lanka Telecommunications Act) to which the Department of Telecommunications (DOT) was entitled or subject to immediately before the transfer date of 1 September 1991 were vested with SLT.

On 25 September 1996, SLT was converted to a public limited company under the Conversion of Public Corporations or Government Owned Business Undertakings into Public Limited Companies Act No. 23 of 1987, vide Extraordinary Gazette No. 942/7 dated 25 September 1996.

On 5 August 1997, the Government of Sri Lanka as the sole shareholder of SLT divested 35% (631,701,000 ordinary shares) of the issued ordinary share capital to Nippon Telegraph and Telephone Corporation (NTT) and entered into an agreement to transfer the management of SLT to NTT. On 2 July 1998, the Government of Sri Lanka divested a further 3.5% of the issued ordinary share capital by transfer of 63,170,010 ordinary shares to the employees of SLT. On 22 March 2000, NTT transferred the entire 35% of their holding in SLT to NTT Communications Corporation (NTT Com).

The Government of Sri Lanka divested further 12% of its holding to the public through a listing on the Colombo Stock Exchange in November 2002, reducing its holding to 49.5%.

On 4 June 2007, SLT was re-registered under the Companies Act No. 07 of 2007 as Sri Lanka Telecom PLC.

### 3. NATURE OF THE BUSINESS OF THE COMPANY AND ITS SUBSIDIARIES

The nature of the business of the Company and its subsidiaries is given in Note 1 to the Group financial statements on page 89.

### 4. FINANCIAL STATEMENTS

The financial statements, which includes the income statement, balance sheet, statement of changes in equity, cash flow statement and the notes to the financial statements of the Group and the Company for the year ended 31 December 2007 are set out on page 84 to 120.

### 5. AUDITORS' REPORT

The Auditors' Report is set out on page 83.

### 6. CHANGES IN ACCOUNTING POLICIES

The accounting policies adopted by the Company and its subsidiaries have been consistently applied from previous years.

**7. REVIEW OF BUSINESS**

The state of affairs of the Group at 31 December 2007 is set out in the balance sheet on page 85. An assessment of the financial performance of the Group and other developments during the financial year is given in the CEO's Review.

**8. PROPERTY, PLANT & EQUIPMENT**

The movements in property, plant & equipment during the year are set out in Note 14 to the Group financial statements.

**9. MARKET VALUE OF PROPERTIES**

The Directors are of the opinion that the carrying amount of properties stated in Note 14 to the Group financial statements reflects their fair value.

**10. GROUP ACTIVITIES**

The Group provides a broad portfolio of telecommunication services across Sri Lanka, the main activity being domestic and international telephone services. In addition, the range of services provided by the Group include, inter alia, Internet services, data services, domestic and international leased circuits, frame relay, ISDN, satellite uplink and maritime transmission.

**11. SUBSIDIARIES**

The Group comprised of the Company and the wholly-owned subsidiaries noted below:

- Mobitel (Private) Limited - Mobile Telecommunication Services
- Sri Lanka Telecom (Services) Limited - Total network solutions
- SLT (Hong Kong) Limited - IP transit services
- SLT Publications (Private) Limited - Directory publication services

**12. DIVIDEND**

The Directors have recommended the payment of a first and final dividend on ordinary shares for the financial year ended 31 December 2007 of Rs. 1 per share (Rs. 1,804,860,000). In accordance with the Sri Lanka Accounting Standard No. 12 (Revised) - Events after Balance Sheet Date, this proposed first and final dividend has not been recognised as a liability as at 31 December 2007.

Taking into account the above distribution, the Board is satisfied that Company meets the solvency test requirement under Section 56 (2) of the Companies Act No. 7 of 2007. The Statutory Auditors have issued a Certificate of Solvency confirming this matter.

**13. RESERVES**

Total reserves and their composition are set out in the statements of changes in equity on pages 86 and 87 of the Group financial statements.

**14. SUBSTANTIAL SHAREHOLDINGS**

As per the share register, following shareholders held more than 5% of the 1,804,860,000 ordinary shares in issue as at 31 December 2007:

	<b>Holding %</b>	<b>No. of Shares</b>
Government of Sri Lanka	49.50	893,405,700
NTT Communications Corporation	35.20	635,076,318

The balance 15.30% shares are held by the public and employees of the Company.

#### 15. INVESTOR RELATIONS

In addition to the Annual General Meetings at which the Directors have a dialogue with the shareholders, timely financial reports are presented to investors on quarterly and annual basis. The Investor Relations Officers together with the Chief Executive Officer (CEO) meet institutional shareholders, rating agencies and fund managers on a regular basis. Additionally, the shareholders and the rating agencies are kept up-to-date on the business endeavours and other activities undertaken by the Group to enhance stakeholder value, through its quarterly newsletter 'Investor'.

#### 16. DIRECTORS

During the year nine Directors held office. At 31 December 2007, the Board of the Company comprised the following Directors:

Mr. P. Asoka Weerasinghe De Silva - *Chairman*  
Mr. Shoji Takahashi - *CEO*  
Mr. Shuhei Anan  
Mrs. Leisha Chandrasena  
Mr. S.N. Kumar  
Mr. Sumith Wijesinghe  
Mr. P.A. Abeysekera - *Appointed on 31 August 2007*

The following Directors resigned from the Board:

Mr. S.B. Divaratne - *Resigned on 4 May 2007*  
Mr. Jun Sawada - *Resigned on 16 January 2007*

The Board wishes to place on record their sincere appreciation of the services rendered by Mr. S.B. Divaratne and Mr. Jun Sawada during their tenure on the Board.

#### Re-election of Directors

The Article 91 of the Articles of Association require that one-third of the Directors or a number nearest thereto retire at each Annual General Meeting and offer themselves for re-election.

Accordingly, Mrs. Leisha Chandrasena and Mr. S.N. Kumar retired from the Board on 31 December 2007. Being eligible they offer themselves for re-election.

During the year Mr. P.A. Abeysekera who was appointed to fill a casual vacancy on the Board. In terms of Article 97, of the Articles of Association, he is required to retire at end of the financial year. Being eligible, he offer himself for election.

#### 17. DIRECTORS' INTERESTS IN CONTRACTS AND PROPOSED CONTRACTS WITH THE COMPANY

The Directors' interests in contracts and proposed contracts with the Company, both direct and indirect, are set out in Note 33 to the group financial statements. Where necessary, the Directors have disclosed the nature of their interests in contracts and proposed contracts.

#### 18. REMUNERATION AND OTHER BENEFITS OF DIRECTORS

The remuneration and other benefits of Directors are given in Note 5 to the Group financial statements on page 101.

#### 19. DIRECTORS' INTERESTS IN SHARES OF THE COMPANY

As at 31 December 2007 none of the Directors held shares of the Company.

#### 20. AMOUNTS PAYABLE TO THE FIRM HOLDING OFFICE AS AN AUDITOR

The remuneration payable by the Company to independent auditors is given in Note 5 to the financial statements on page 101.

**21. AUDITOR'S RELATIONSHIP OR ANY INTEREST WITH THE COMPANY**

The Directors are satisfied that, based on written representations made by the Independent Auditors to the Board, the auditors did not have any relationship or any interest with the Company and its subsidiaries that would impair their independence.

**22. CORPORATE GOVERNANCE**

The business and affairs of the Group are managed and directed with the objective of balancing the attainment of corporate objectives with the alignment of corporate behaviour within the legal and the good governance framework of the industry and Sri Lanka, the accountability to shareholders and responsibility to other stakeholders.

To achieve corporate governance objectives the Board has set up Board Sub-Committees to exercise oversight in specific areas. During the year the Audit Committee comprised of Mrs. Leisha Chandrasena and Mr. S.N. Kumar.

**23. STATUTORY PAYMENTS**

All statutory payments due to the Government of Sri Lanka and on behalf of employees have been made or accrued for at the balance sheet date.

**24. ENVIRONMENTAL PROTECTION**

After making adequate enquiries from management, the Directors are satisfied that the Company operates in a manner that minimises the detrimental effects on the environment and provides products and services that have a beneficial effect on the customers and the communities within which the Group operates.

**25. DONATIONS**

During the year the Directors had approved donations amounting to Rs. 575,000/- and none of them were to any approved charity.

**26. GOING CONCERN**

The financial statements are prepared on going concern principles. After making adequate enquiries from management, the Directors are satisfied that the Group has adequate resources to continue its operations in the foreseeable future.

**27. FUTURE DEVELOPMENTS**

In keeping with current global dynamics in the industry the Group intends to transform itself from a traditional telecommunications service provider to a global communication solutions provider. In reaching towards this goal, the value added services that the Group intends to offer its customers include, inter alia, IP TV, Wi-Max, Web Calling, IVR Services and Hosted PABX Services.

**28. POST BALANCE SHEET EVENTS**

No events had occurred since the balance sheet date and the approval of these financial statements, which would require adjustments to, or disclosure in these Group financial statements.

**29. APPOINTMENT OF AUDITORS**

A resolution to reappoint the Auditors, Messrs. PricewaterhouseCoopers, Chartered Accountants, who have expressed their willingness to continue, will be proposed at the Annual General Meeting.

By Order of the Board

**Asoka Weerasinghe de Silva**  
*Director*

**Shoji Takahashi**  
*Director*

**P.G. Dias**  
*Secretary*

Colombo  
11 February 2008

## STATEMENT OF THE DIRECTORS' RESPONSIBILITY FOR THE PREPARATION OF FINANCIAL STATEMENTS

The responsibility of the Directors in relation to the financial statements of the Company and the Group, is set out in the following statement. The responsibility of the Auditors, in relation to the financial statements, prepared in accordance with the provision of the Companies Act No. 07 of 2007 [‘the Act’], is set out in the Independent Auditors' Report on page 83.

The financial statements comprise of:

- Income Statements, which present a true and fair view of the profit and loss of the Company and the Group for the financial year; and
- Balance Sheets, which present a true and fair view of the state of affairs of the Company and the Group as at the end of the financial year, and which comply with the requirements of the Act.

The Directors are required to ensure that, in preparing these financial statements:

- appropriate accounting policies have been selected and applied in a consistent manner and material departures, if any, have been disclosed and explained;
- all applicable Accounting Standards issued by the Institute of Chartered Accountants of Sri Lanka, as relevant, have been followed;
- judgements and estimates have been made which are reasonable and prudent.

The Directors are also required to ensure that the Company has adequate resources to continue in operation to justify applying the going concern basis in preparing these financial statements.

Further, the Directors have a responsibility to ensure that the Company maintains sufficient accounting records to disclose, with reasonable accuracy the financial position of the Company and of the Group, and to ensure that the financial statements presented comply with the requirements of the Act.

The Directors are also responsible for taking reasonable steps to safeguard the assets of the Company and of the Group and in this regard to give proper consideration to the establishment of appropriate internal control systems with a view to preventing and detecting fraud and other irregularities.

Our Internal Auditors have conducted periodic audits to provide reasonable assurance that the established policies and procedures of the Company were consistently followed. However, there are inherent limitations that should be recognised in weighing the assurances provided by any system of internal controls and accounting.

The Audit Committee of the Company meets periodically with the Internal Auditors and the Independent Auditors to review the manner in which these auditors are performing their responsibilities, and to discuss auditing, internal control and financial reporting issues. To ensure complete independence, the Independent Auditors and the Internal Auditors have full and free access to the members of the Audit Committee to discuss any matter of substance.

The Directors are required to prepare the financial statements and to provide the Independent Auditors with every opportunity to take whatever steps and undertake whatever inspections that may consider to be appropriate to enable them to give the Independent Auditors' opinion.

The Directors are of the view that they have discharged their responsibilities as set out in this statement.

### COMPLIANCE REPORT

The Directors confirm that to the best of their knowledge, all taxes, duties and levies payable by the Company and its Subsidiaries, all contributions, levies and taxes payable on behalf of and in respect of the Employees of the Company and its Subsidiaries, and all other known statutory dues as were due and payable by the Company and its Subsidiaries as at the balance sheet date have been paid, or where relevant provided for, except as specified in Note 32 to the financial statements covering contingent liabilities.

By Order of the Board

*Secretary*  
Colombo  
11 February 2008



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**TO THE MEMBERS OF SRI LANKA TELECOM PLC  
 REPORT ON THE FINANCIAL STATEMENTS**

We have audited the accompanying consolidated financial statements of Sri Lanka Telecom PLC and its subsidiaries, which comprise the balance sheet as at 31 December 2007, the income statement, the statement of changes in equity and the cash flow statement for the year then ended, and a summary of significant accounting policies and other explanatory notes as set out on pages 84 to 120.

**Management's Responsibility for the Financial Statements**

Management is responsible for the preparation and fair presentation of these financial statements in accordance with Sri Lanka Accounting Standards. This responsibility includes: designing, implementing and maintaining internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

**Scope of Audit and Basis of Opinion**

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with Sri Lanka Auditing Standards. Those standards require that we plan and perform the audit to obtain reasonable assurance whether the financial statements are free from material misstatement.

An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the

accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

We have obtained all the information and explanations which to the best of our knowledge and belief were necessary for the purposes of our audit. We therefore believe that our audit provides a reasonable basis for our opinion.

**Opinion**

In our opinion, so far as appears from our examination, the Company maintained proper accounting records for the year ended 31 December 2007 and the financial statements give a true and fair view of the Company's state of affairs as at 31 December 2007 and of its results for the year and cash flows for the year then ended in accordance with Sri Lanka Accounting Standards.

In our opinion, the consolidated financial statements give a fair view of the state of affairs as at 31 December 2007 and consolidated results for the year and cash flows for the year then ended, in accordance with Sri Lanka Accounting Standards, of the Company and its subsidiaries dealt with thereby, so far as concern the members of the Company.

**Report on Other Legal & Regulatory Requirements**

These financial statements also comply with the requirements of Sections 153 (2) to 153 (7) as appropriate of the Companies Act No. 07 of 2007.

**PricewaterhouseCoopers**  
 Chartered Accountants

Colombo  
 11 February 2008

Partners Y. Kanagasabai FCA, D.T.S.H. Mudalige FCA, S. Manoharan ACA, S. Gajendran FCA, N.R. Gunasekara FCA,  
 Ms. S. Hadgie FCA, Ms. S. Perera ACA

## CONSOLIDATED INCOME STATEMENT

*(All amounts in Sri Lanka Rupees millions)  
For the year ended 31 December 2007*

	Notes	Group		Company	
		2007	2006	2007	2006
Revenue	4	<b>43,234</b>	40,691	<b>37,068</b>	36,109
Operating costs	5	<b>(20,748)</b>	(17,915)	<b>(17,231)</b>	(15,351)
Operating profit before depreciation amortisation and ITL		<b>22,486</b>	22,776	<b>19,837</b>	20,758
Depreciation	14	<b>(10,220)</b>	(9,964)	<b>(8,884)</b>	(8,808)
Amortisation of intangible assets	15	<b>(196)</b>	(210)	<b>(94)</b>	(89)
International Telecommunication Operators' Levy (ITL)	7	<b>(2,851)</b>	(2,282)	<b>(2,727)</b>	(2,280)
Operating profit		<b>9,219</b>	10,320	<b>8,132</b>	9,581
Voluntary Retirement Scheme (VRS) cost	8	<b>(43)</b>	(425)	<b>(43)</b>	(425)
Other income		<b>169</b>	180	<b>166</b>	175
Interest expense and finance costs	9	<b>(2,232)</b>	(1,884)	<b>(1,363)</b>	(1,268)
Interest income	10	<b>1,286</b>	1,036	<b>1,239</b>	1,166
Profit before tax		<b>8,399</b>	9,227	<b>8,131</b>	9,229
Tax	11	<b>(2,759)</b>	(3,789)	<b>(2,743)</b>	(3,732)
<b>Net profit</b>		<b>5,640</b>	5,438	<b>5,388</b>	5,497
<b>Attributable to:</b>					
Equity holders of the Company		<b>5,640</b>	5,438		
Earnings per share of profit attributable to equity holders of the Company					
Basic (Rs.)	12	<b>3.12</b>	3.01	<b>2.99</b>	3.05

All of the Group's activities are continuing activities.

*The Notes on pages 89 to 120 form an integral part of these financial statements.*

*Report of the Auditors on page 83.*

## CONSOLIDATED BALANCE SHEET

(All amounts in Sri Lanka Rupees millions)  
As at 31 December 2007

	Notes	Group		Company	
		2007	2006	2007	2006
<b>ASSETS</b>					
<b>Non-current assets</b>					
Property, plant & equipment	14	53,881	54,202	41,350	44,633
Intangible assets	15	1,614	1,588	376	260
Investments in subsidiaries	16	–	–	7,782	7,032
Non-current receivables	17	1,268	960	1,268	960
		<b>56,763</b>	56,750	<b>50,776</b>	52,885
<b>CURRENT ASSETS</b>					
Inventories	18	1,476	1,419	1,373	1,325
Receivables and prepayments	19	9,938	10,558	10,064	10,554
Cash & cash equivalents	20	17,195	15,315	16,689	14,390
		<b>28,609</b>	27,292	<b>28,126</b>	26,269
<b>Total assets</b>		<b>85,372</b>	84,042	<b>78,902</b>	79,154
<b>EQUITY AND LIABILITIES</b>					
<b>Capital and reserves</b>					
Stated capital	28	18,049	18,049	18,049	18,049
Hedging reserve	29	(58)	(236)	(58)	(236)
Insurance reserve	26	204	183	204	183
Retained earnings		23,705	19,870	26,288	22,705
		<b>41,900</b>	37,866	<b>44,483</b>	40,701
Deferred income	23	6,429	7,110	6,429	7,110
<b>Non-current liabilities</b>					
Grants		68	75	68	75
Deferred income tax liabilities	22	2,777	4,513	2,777	4,513
Borrowings	21	16,660	16,868	12,366	13,065
Retirement benefit obligations	25	1,329	942	1,272	903
Trade and other payables	24	279	298	279	298
		<b>21,113</b>	22,696	<b>16,762</b>	18,854
<b>Current liabilities</b>					
Trade and other payables	24	11,409	8,721	8,537	7,330
Current tax liabilities		1,896	3,732	1,858	3,705
Borrowings	21	2,625	3,917	833	1,454
		<b>15,930</b>	16,370	<b>11,228</b>	12,489
<b>Total liabilities</b>		<b>37,043</b>	39,066	<b>27,990</b>	31,343
<b>Total equity and liabilities</b>		<b>85,372</b>	84,042	<b>78,902</b>	79,154

These financial statements were approved by the Board of Directors on 8 February 2008 and were signed on its behalf by:

(Sgd.)  
**P. Asoka Weerasinghe de Silva**  
Director

(Sgd.)  
**Shoji Takahashi**  
Director

(Sgd.)  
**P.M.A. Sirimane**  
Chief Financial Officer

The Notes on pages 89 to 120 form an integral part of these financial statements.

Report of the Auditors on page 83.

## CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

(All amounts in Sri Lanka Rupees millions)

For the year ended 31 December 2007

	Notes	Stated capital	Hedging reserve	Insurance reserve	Capital reserve	Retained earnings	Total
<b>GROUP</b>							
<b>Year ended 31 December 2006</b>							
<b>Balance at 1 January 2006</b>		18,049	(208)	166	188	15,598	33,793
Hedging reserve	29						
- foreign currency translation difference		-	(96)	-	-	-	(96)
- charged to income statement		-	68	-	-	-	68
Insurance reserve							
- charged to income statement	26	-	-	17	-	-	17
Capital reserve							
- transferred to retained earnings		-	-	-	(188)	188	-
Dividend for 2005	13	-	-	-	-	(1,354)	(1,354)
Net profit for the year 2006		-	-	-	-	5,438	5,438
<b>Balance at 31 December 2006</b>		<b>18,049</b>	<b>(236)</b>	<b>183</b>	<b>-</b>	<b>19,870</b>	<b>37,866</b>
<b>Year ended 31 December 2007</b>							
<b>Balance at 1 January 2007</b>		<b>18,049</b>	<b>(236)</b>	<b>183</b>	<b>-</b>	<b>19,870</b>	<b>37,866</b>
Hedging reserve	29						
- foreign currency translation difference		-	(17)	-	-	-	(17)
- charged to income statement		-	195	-	-	-	195
Insurance reserve							
- charged to income statement	26	-	-	21	-	-	21
Dividend for 2006	13	-	-	-	-	(1,805)	(1,805)
Net profit for the year 2007		-	-	-	-	5,640	5,640
<b>Balance at 31 December 2007</b>		<b>18,049</b>	<b>(58)</b>	<b>204</b>	<b>-</b>	<b>23,705</b>	<b>41,900</b>

The Notes on pages 89 to 120 form an integral part of these financial statements.

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## STATEMENT OF CHANGES IN EQUITY

(All amounts in Sri Lanka Rupees millions)

For the year ended 31 December 2007

	Notes	Stated capital	Hedging reserve	Insurance reserve	Capital reserve	Retained earnings	Total
<b>COMPANY</b>							
<b>Year ended 31 December 2006</b>							
<b>Balance at 1 January 2006</b>		18,049	(208)	166	188	18,374	36,569
Hedging reserve	29						
- foreign currency translation difference		-	(96)	-	-	-	(96)
- charged to income statement		-	68	-	-	-	68
Insurance reserve							
- charged to income statement	26	-	-	17	-	-	17
Capital reserve							
- transferred to retained earnings		-	-	-	(188)	188	-
Dividend for 2005	13	-	-	-	-	(1,354)	(1,354)
Net profit for the year 2006		-	-	-	-	5,497	5,497
<b>Balance at 31 December 2006</b>		<b>18,049</b>	<b>(236)</b>	<b>183</b>	<b>-</b>	<b>22,705</b>	<b>40,701</b>
<b>Year ended 31 December 2007</b>							
<b>Balance at 1 January 2007</b>		<b>18,049</b>	<b>(236)</b>	<b>183</b>	<b>-</b>	<b>22,705</b>	<b>40,701</b>
Hedging reserve	29						
- foreign currency translation difference		-	(17)	-	-	-	(17)
- charged to income statement		-	195	-	-	-	195
Insurance reserve							
- charged to income statement	26	-	-	21	-	-	21
Dividend for 2006	13	-	-	-	-	(1,805)	(1,805)
Net profit for the year 2007		-	-	-	-	5,388	5,388
<b>Balance at 31 December 2007</b>		<b>18,049</b>	<b>(58)</b>	<b>204</b>	<b>-</b>	<b>26,288</b>	<b>44,483</b>

The Notes on pages 89 to 120 form an integral part of these financial statements.

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## CONSOLIDATED CASH FLOW STATEMENT

(All amounts in Sri Lanka Rupees millions)  
For the year ended 31 December 2007

	Notes	Group		Company	
		2007	2006	2007	2006
<b>Operating activities</b>					
Cash generated from operations	30	22,003	19,337	17,854	16,248
Interest received		1,684	574	1,637	704
Interest paid		(2,265)	(2,142)	(1,396)	(1,470)
Tax paid		(6,332)	(4,334)	(6,326)	(4,284)
<b>Net cash generated from operating activities</b>		<b>15,090</b>	<b>13,435</b>	<b>11,769</b>	<b>11,198</b>
<b>Investing activities</b>					
Acquisition of property, plant & equipment		(9,866)	(8,033)	(5,568)	(5,897)
Acquisition of intangible assets	15	(222)	(1,168)	(210)	(202)
Proceeds from disposal of property, plant & equipment		15	4	15	4
Loan given to subsidiary - 2006		-	-	-	(500)
Investments in subsidiaries	16	-	-	(750)	(535)
<b>Net cash used in investing activities</b>		<b>(10,073)</b>	<b>(9,197)</b>	<b>(6,513)</b>	<b>(7,130)</b>
<b>Financing activities</b>					
Proceeds from borrowings		2,653	-	-	-
Finance lease principal payments		(4)	-	(4)	-
Re-payment of borrowings		(3,399)	(3,739)	(1,271)	(1,821)
Dividends paid	13	(1,805)	(1,354)	(1,805)	(1,354)
<b>Net cash used in financing activities</b>		<b>(2,555)</b>	<b>(5,093)</b>	<b>(3,080)</b>	<b>(3,175)</b>
<b>Increase/(decrease) in cash and cash equivalents</b>		<b>2,462</b>	<b>(855)</b>	<b>2,176</b>	<b>893</b>
<b>Movement in cash and cash equivalents</b>					
Cash & cash equivalents at beginning of year (Note 20)		14,335	14,428	14,390	12,735
Effect of exchange fluctuation on cash & cash equivalents		123	762	123	762
		14,458	15,190	14,513	13,497
Increase/(decrease)		2,462	(855)	2,176	893
<b>At end of year</b>	20	<b>16,920</b>	<b>14,335</b>	<b>16,689</b>	<b>14,390</b>

The Notes on pages 89 to 120 form an integral part of these financial statements.

Report of the Auditors on page 83.

**1. GENERAL INFORMATION**

Sri Lanka Telecom PLC was incorporated under the Companies Act No. 17 of 1982 on 25 September 1996 and re-registered on 4 June 2007 under the Companies Act No. 7 of 2007, that came into effect from 3 May 2007. The registered office of the Company is situated at Lotus Road, Colombo 1. The Company is a quoted public company which has its listing on the Colombo Stock Exchange.

The Group provides a broad portfolio of telecommunication services across Sri Lanka, the main activity being domestic and international telephone services. In addition, the range of services provided by the Group include, inter alia, internet services, data services, domestic and international leased circuits, frame relay, ISDN, satellite uplink and maritime transmission.

The consolidated financial statements have been approved for issue by the Board of Directors on 8 February 2008.

**2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

The principal accounting policies applied in the preparation of these consolidated financial statements are set out below. These policies have been consistently applied to all the years presented, unless stated otherwise.

**2.1 Basis of preparation**

The consolidated financial statements are prepared in accordance and comply with Sri Lanka Accounting Standards. The consolidated financial statements are prepared under the historical cost convention. Where any item is not covered by Sri Lanka Accounting Standards (SLASs), International Financial Reporting Standards (IFRSs) are followed except for IAS 32 (Financial Instruments: Presentation), IAS 39

(Financial Instruments: Recognition and Measurement) and IFRS 7 (Financial Instruments: Disclosures) that have not been adopted in Sri Lanka.

The preparation of financial statements in conformity with SLASs & IFRSs requires the use of certain critical accounting estimates. It requires management to exercise their judgement in the process of applying the Company's accounting policies.

**2.2 Consolidation**

Subsidiaries are all entities (including special purpose entities) over which a Company has the power to govern the financial and operating policies that is generally accompanied by a shareholding of more than one half of the voting rights. The existence and effect of potential voting rights that are currently exercisable or convertible are considered when assessing whether the Company controls another entity. Subsidiaries are fully consolidated from the date on which control is transferred. They are de-consolidated from the date that control ceases.

The purchase method of accounting is used to account for the acquisition of subsidiaries by the Company. The cost of an acquisition is measured as the fair value of the assets given, equity instruments issued and liabilities incurred or assumed at the date of exchange, plus costs directly attributable to the acquisition. The excess of the cost of acquisition over the fair value of the Group's share of the identifiable net assets acquired is recorded as goodwill. If the cost of acquisition is less than the fair value of the net assets of the subsidiary acquired, the difference is recognised directly in the income statement.

## NOTES TO THE FINANCIAL STATEMENTS

The inter-Company transactions, balances and unrealised gains on transactions between Group Companies are eliminated. The unrealised losses are also eliminated but considered as an impairment indicator of the asset transferred.

### 2.3 Segment Reporting

A business segment is a group of assets and operations subject to risks and returns that are different from those of other business segments. A geographical segment is engaged in providing products or services within a particular economic environment that are subject to risks and returns which are different from those of segments operating in other economic environments. All business segments which account for more than 10% of the total Group revenue are separately reported. (See Note 3)

### 2.4 Foreign currency translations

#### (a) *Functional and presentation currency*

The items included in the financial statements of each of the Group's entities are measured using the currency of the primary economic environment in which the entity operates ('the functional currency'). The consolidated financial statements are presented in Sri Lanka Rupees, which is the Company's functional and presentation currency.

#### (b) *Transactions and balances*

Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the dates of such transactions. The foreign exchange gains and losses resulting from

the settlement of such transactions and from the translation of monetary assets and liabilities denominated in foreign currencies at year end exchange rates are recognised in the income statements.

#### (c) *Group Companies*

The results and financial position of all the Group entities that have a functional currency different from the presentation currency are translated into the presentation currency as follows:

- (i) assets and liabilities for each balance sheet presented are translated at the closing rate of the date of that balance sheet; and
- (ii) income and expenses for each income statement are translated at average exchange rates (unless this average is not a reasonable approximation of the cumulative effect of the rates prevailing on the transaction dates, in which case income and expenses are translated at the rate on the dates of the transactions).

On consolidation, exchange differences arising from the translation of the net investment in foreign operations, and of borrowings and other currency instruments designated as hedges of such investments, are taken to shareholders' equity. When a foreign operation is sold, exchange differences that were recorded in equity are recognised in the income statement as part of the gain or loss on sale.

## NOTES TO THE FINANCIAL STATEMENTS

The goodwill and fair value adjustments arising on the acquisition of a foreign entity are treated as assets and liabilities of the foreign entity and are translated at the closing rate of the date of that balance sheet.

### 2.5 Property, plant & equipment

All property, plant & equipment are stated at historical cost less accumulated depreciation except as noted in Note 14 where property, plant & equipment of Department of Telecommunications were transferred to Sri Lanka Telecom at a valuation performed by the Government of Sri Lanka.

#### (a) Measurement

This historical cost includes all costs directly attributable to bringing an asset to working condition for its intended use and significant renovations. The cost in the case of the telecommunication network comprises all expenditure up to and including the cabling cost within customers' premises and undersea cables.

The subsequent costs are included in the assets carrying amount or recognised as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Group and the cost of the item can be measured reliably. The carrying amounts of the assets replaced are derecognised. All repairs and maintenance are charged to the income statement during the financial period in which they are incurred.

An assets carrying amount is written down immediately to its recoverable amount if the carrying amount is greater than its estimated recoverable amount.

The interest costs on borrowings to finance the construction of property, plant & equipment are capitalised as part of the cost of the asset, during the period that is taken to complete and prepare the asset for its intended use.

#### (b) Depreciation

The freehold land is not depreciated. The depreciation on other assets is calculated using the straight-line method to allocate their cost or revalued amounts to their residual values over the estimated useful lives, as follows:

Asset category	Useful life
Freehold buildings	40 years
Ducts cables and other outside plant	10 to 12.5 years
Undersea cables	10 years
Telephone exchanges and transmission equipment	10 to 12.5 years
Motor vehicles	5 years
Other fixed assets	4 to 10 years

#### (c) Disposal

The gains and losses on disposals are determined by comparing proceeds with carrying amount. These are included in the income statement.

## 2.6 Intangible Assets

### (a) Goodwill

The goodwill represents the excess of the cost of an acquisition over the fair value of the Group's shares of the net identifiable assets of the acquired subsidiary at the date of acquisition. The goodwill on acquisitions of subsidiaries is included in intangible assets. The separately recognised goodwill is tested annually for impairment and carried at cost less accumulated impairment losses. The impairment losses on goodwill are not reversed.

### (b) Licences

The licence are recognised at historical cost. The licences that have a finite useful life is carried at cost less accumulated amortisation. The amortisation is calculated using the straight-line method to allocate the cost over the period of the licence.

### (c) Computer Software

The acquired computer software licences are recognised at cost incurred to acquire and bring to use the specific software application. These costs are amortised over their estimated useful lives (5 years).

The costs associated with developing or maintaining computer software programmes are recognised as an expense when incurred. The costs that are directly associated with the development of identifiable and unique software products controlled by the Group, and that will probably generate economic benefits exceeding costs

beyond one year, are recognised as intangible assets. Such software costs include the software development, employee salaries and an appropriate portion of relevant overheads.

The computer software costs recognised as intangible assets are amortised over their estimated useful lives (not exceeding 5 years).

### (d) Deferred Insurance Premium

The insurance premium paid by the Company to secure foreign loans under the 150K Project Scheme has been deferred on the basis that the benefit of this expenditure is not exhausted in the period in which it was incurred. This insurance premium is amortised over the loan repayment period of 10 years.

## 2.7 Grants

The grants relating to property, plant & equipment are included in non-current liabilities and are credited to the income statement on a straight-line basis over the expected useful lives of the related assets.

## 2.8 Impairment of Non-Financial Assets

The assets that have an indefinite useful life, for example goodwill, are not subject to amortisation. They are tested annually for impairment. The assets that are subject to amortisation are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An impairment loss is recognised for the amount by which the assets carrying amount exceeds its recoverable amount. The recoverable amount is the higher of an asset's

fair value less costs to sell and value in use. For the purposes of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash flows (cash-generating units). Non-financial assets other than goodwill that suffered an impairment are reviewed for possible reversal of the impairment at each reporting date.

### **2.9 Investments**

The long-term investments are initially recognised at cost and provision is only made where, in the opinion of the Directors, there is a permanent diminution in value. Where there has been a permanent diminution in the value of an investment, it is recognised as an expense in the period in which the diminution is identified.

On disposal of an investment, the difference between the net disposal proceeds and the carrying amount is charged or credited to the income statement.

### **2.10 Inventories**

All inventories are held for the provision of service by the Group. The inventories are stated at the lower of cost and net realisable value. For this purpose, the cost of inventories is determined using the Weighted Average Cost (WAC). The cost of inventories include all costs of purchase, costs of conversion and other costs incurred in bringing the inventories to their present location and condition.

Net realisable value is the estimated selling price in the ordinary course of business, less applicable variable selling expenses.

Provision is made for slow-moving and obsolete inventories, which are not expected to be used internally.

### **2.11 Trade receivables**

The trade receivables are recognised initially at cost and subsequently carried at cost less provision for impairment. A provision for impairment of trade receivables is established when there is objective evidence that the Group will not be able to collect all amounts due according to the original terms of the receivables. The amount of the provision is the difference between the asset's carrying amount and the present value of estimated future cash flows. The carrying amount of the asset is reduced through the use of an allowance account. Once decided as irrecoverable after due recovery procedures, the amount of the loss is recognised as an operating cost in the income statement. When a trade receivable is uncollectible, it is written off against the allowance account. Subsequent recoveries of amounts previously written off are credited against 'operating costs' in the income statement.

### **2.12 Cash and cash equivalents**

Cash and cash equivalents includes cash in hand, deposits held at call with banks, other short-term highly liquid investments with original maturities of three months or less, net of bank overdrafts. Bank overdrafts are shown within borrowings in current liabilities on the balance sheet.

### **2.13 Stated Capital**

The ordinary shares are classified as equity.

### **2.14 Insurance Reserve**

The Company transfers annually from the income statement an amount equal to 0.1% of additions to property, plant & equipment to an insurance reserve. An equal amount is invested in a sinking fund to meet any funding requirements for potential losses from uninsured property, plant & equipment.

**2.15 Trade Payables**

The trade payables are recognised at fair value.

**2.16 Borrowings**

The borrowings are recognised initially at fair value, net of transaction costs incurred. The borrowings are subsequently stated at amortised cost. Any difference between the proceeds (net of transaction costs) and the redemption value is recognised in the income statement over the period of the borrowings using the effective interest method.

The borrowings are classified as current liabilities unless the Group has an unconditional right to defer settlement of the liability for at least 12 months after the balance sheet date.

**2.17 Leases**

A lease is an agreement whereby the lessor conveys to the lessee in return for a payment, or series of payments, the right to use an asset for an agreed period of time.

**(a) Finance Lease**

The Group leases certain motor vehicles included in property, plant and equipment. The leases where the Group has substantially all the risks and rewards are classified as finance leases. The finance leases are capitalised, at the lessees commencement at the lower of the fair value of the leased assets and present value of the minimum lease payments. Each lease payment is allocated between the liability and finance charges so as to achieve a constant rate on the finance lease balance outstanding. The corresponding rental

obligations, net of finance charges, are included in long-term payables. The interest element of the finance lease is charged to the income statement over the lease period so as to produce a constant periodic rate of interest on the remaining balance of the liability for each period. The plant and equipment acquired under finance leases is depreciated over the shorter of the useful life of the asset or the lease term.

**(b) Operating Lease**

The leases in which a significant portion of the risks and rewards of ownership are retained by the lessor are classified as operating leases. The payments made under operating leases (net of any incentives received from the lessor) are charged to the income statement on a straight-line basis over the period of the lease.

**2.18 Current and Deferred Income Tax**

The current income tax charge is calculated on the basis of the tax laws enacted or substantially enacted at the balance sheet date in the countries where the Company and its subsidiaries generate taxable income. Management periodically evaluates positions taken in tax returns with respect to situations in which applicable tax regulations are subject to interpretation and establishes provisions where appropriate on the basis of amounts expected to be paid to the tax authorities.

Deferred income tax is provided in full, using the liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the financial statements. However, the deferred income tax is not accounted for if it arises from initial recognition of an asset or liability

## NOTES TO THE FINANCIAL STATEMENTS

in a transaction other than in a business combination, that at the time of the transaction, affects neither accounting nor taxable profit or loss. Deferred income tax is determined using tax rates (and laws) that have been enacted or subsequently enacted by the balance sheet date and are expected to apply when the related deferred income tax asset is realised or the deferred income tax liability is settled.

Deferred income tax assets are recognised to the extent that it is probable that future taxable profit will be available against which the temporary differences can be utilised.

Deferred income tax is provided on temporary differences arising from investments in subsidiaries except where the timing of the reversal of the temporary difference is controlled by the Group and it is probable that the temporary difference will not reverse in the foreseeable future.

### 2.19 Employee benefits

The Group has both defined benefit and defined contribution plans.

#### (a) *Defined contribution plan*

All employees of the Company are members of the Sri Lanka Telecom Provident Fund and the Employees' Trust Fund (ETF) to which the Company contributes 15% and 3% respectively of such employees' basic salary and allowances. All employees of subsidiaries of the Group except for SLT (Hong Kong) Limited are members of Employees' Provident Fund (EPF) and Employees' Trust Fund (ETF), to which

respective subsidiaries contribute 15% and 3%, respectively, of such employees' basic salary and allowances.

The Company has no further payment obligations once the contributions have been paid. The contributions are recognised as employee benefit expenses when they are due.

#### (b) *Defined benefit plan*

Typically, a defined benefit plan defines an amount of benefit that an employee will receive on retirement, which is, usually a dependent on one or more factors such as period of service and compensation.

The liability recognised in the balance sheet in respect of defined benefit plans is the present value of the defined benefit obligation at the balance sheet date together with adjustments for unrecognised gains or losses and past service costs. The defined benefit obligation is calculated annually by independent actuaries using the projected unit credit method. The present value of defined benefit obligation is determined by discounting the estimated future cash outflows using estimated long-term interest rates.

The actuarial gains and losses are charges or credited to income statement in the period in which they arise.

The assumptions, based on which the results of the actuarial valuation were determined, are included in Note 25 to the Group financial statements.

## 2.20 Provisions

A provision is recognised when the Group has a present legal or constructive obligation as a result of past events, it is more likely than not, that an outflow of resources will be required to settle the obligation and the amount has been reliably estimated. Provisions are not recognised for future operating losses.

Where there are a number of similar obligations, the likelihood that an outflow will be required in settlement is determined by considering the class of obligations as a whole. A provision is recognised even if the likelihood of an outflow with respect to any one item included in the same class of obligation may be small.

The provision are measured at the present value of the expenditures expected to be required to settle the obligation.

## 2.21 Revenue recognition

Revenue comprises the fair value of the consideration received or receivable for services rendered in the ordinary course of business. Revenue is shown net of value added tax, rebates and discounts and after eliminating sales within the Group.

The Group recognises revenue when the amount of revenue can be reliably measured, it is probable that future economic benefits will flow to the entity and when specific criteria have been met for each of the Group's activities as described below. The amount of revenue is not considered to be reliably measurable until all contingencies relating to the sale have been resolved. The Group bases its revenue estimates on historical results,

taking into consideration the types of the transactions and past trends. The revenue is recognised as follows:

(i) ***Domestic and international call revenue and rental income***

The customers are charged for the usage and a monthly fixed rental for the telephony services. The billing cycle is based on the calendar month. The customers are charged Government taxes at the applicable rates. The revenue is recognised net of such taxes.

(ii) ***Revenue from other network operators and international settlements***

The revenue received from other network operators, local and international, for the use of the Group's telecommunication network for completing call connections are recognised, net of taxes, based on traffic minutes/per second rates stipulated in the relevant agreements and regulations.

(iii) ***Revenue from other telephony services***

The revenue from other telephony services are recognised on an accrual basis based on the usage.

(iv) ***Connection fees***

The connection fees relating to Public Switched Telephone Network (PSTN) are deferred over a period of 15 years.

The connection fees relating to Code Divisional Multiple Access (CDMA) connections are recognised as revenue in the period in which the connection is activated.

**(v) Equipment sales**

Revenue from sale of equipment is recognised, net of taxes, on completion of the transaction. The cost of CDMA handsets are recovered through the CDMA connection fees. The CDMA handset remains the property of the Company. However, the cost of the handset is included in operating costs in the period which the connection is activated.

**(vi) Prepaid card revenue**

The revenue from sale of prepaid cards is recognised in the period in which the card is sold. Due to the short validity period after activation, no adjustment is made to revenue for unused airtime at the balance sheet date.

**(vii) Interest income**

Interest income is derived from short-term investment of excess funds and is recognised on an accrual basis.

**(viii) Dividend income**

Dividend income is recognised when the right to receive the payment is established.

**2.22 Expenditure**

The expenses are recognised on accrual basis. All expenditure incurred in the ordinary cause of business and in maintaining property, plant & equipment in a state of efficiency is charged against income in arriving at the profit for the year.

For the purpose of presentation of the income statement information, nature of expense method is used to classify expenses.

**2.23 Foreign currency risk**

The Company hedges foreign currency risk of loans denominated in foreign currency against foreign currency revenue streams such as interest income from foreign currency fixed deposits and receipt from international network operations.

The Company hedges between 50% to 75% of anticipated net foreign earnings for 5 years. Management estimate approximately 75% (2006 - 75%) of projected foreign earnings quality as 'highly probable'.

**2.24 Credit risk**

Credit risk arises from cash and cash equivalents, deposits with banks as well as credit exposure to customers and other network operators including outstanding receivables. For bank and financial institutions only rated financial institutions are accepted. The credit control assess the credit quality of customers, taking into account their financial position, past experience and other factors. The individual risk limits are set based on internal ratings in accordance with limits set by the Boards. The utilisation of credit limits are regularly monitored.

**2.25 Liquidity risk**

Effective liquidity risk management includes maintaining sufficient cash and marketable securities and the availability of funding from an adequate amount of committed credit facilities. Due to dynamic nature of the underlying business, the Group maintains flexibility in funding by maintaining sufficient cash reserves and committed credit lines.

## NOTES TO THE FINANCIAL STATEMENTS

### 2.26 Interest rate risk

The Group's income and operating cash flows are substantially independent of changes in market interest rates.

The Group's interest rate risk arises from long-term borrowings. The borrowings at variable rates expose the Group to cash flow interest rate risk whilst borrowings at fixed rates exposes the Group to fair value interest rate risk. The Group analyses its interest rate exposure on a dynamic basis. Various scenarios are simulated taking into consideration refinancing, renewal of existing positions, alternative financing and hedging.

### 2.27 Dividend distribution

The dividend is recognised as a liability in the financial statements in the period in which the dividends are approved by the Company's shareholders.

### 2.28 Comparatives

The software owned by the Company which were previously disclosed as 'other fixed assets' under property plant and equipment, are now included in 'intangible assets'.

Further, the amortisation of deferred insurance premium which was previously disclosed under finance costs and amortisation of software which was previously disclosed under depreciation are included in 'amortisation of intangible assets' in the income statement.

Management believes that the above re-classifications give a fairer presentation.

## NOTES TO THE FINANCIAL STATEMENTS

(All amounts in Sri Lanka Rupees millions)

### 3. SEGMENT ANALYSIS

#### (a) Primary reporting format - business segments

The Group provides telecommunication services, mainly in Sri Lanka. The Group is organised into five main business segments as follows:

Public Switched Telephone Network - PSTN  
 Code Divisional Multiple Access - CDMA  
 Other network operators  
 Mobile telephony operations  
 Other value added services

The connection charges, rental and call charges derived from fixed wired lines are included in PSTN revenue. Similar revenue streams generated from fixed wireless connections are shown under CDMA revenue. Income derived from local and international operators for use of telecommunication network of the Company is shown as revenue from other network operators. Mobile revenue consist of revenue generated from mobile telephony operations. Other value added services comprise data services, IP & Broad band and other telephony services.

The revenue from each business segment is as follows:

	Group	
	2007	2006
PSTN revenue	18,241	20,529
CDMA revenue	6,188	5,520
Revenue from other network operators	8,253	6,635
Revenue from Mobile telephony operations	5,397	4,165
Revenue from other value added services	6,100	4,650
	44,179	41,499
Inter-segmental revenue	(945)	(808)
Total revenue	43,234	40,691

#### (b) Secondary reporting format - geographical segments

The Group's five main business segments operates in one main geographical area, hence do not qualify for secondary reporting.

## NOTES TO THE FINANCIAL STATEMENTS

### 4. REVENUE

The significant categories under which revenue is recognised are as follows:

	Group		Company	
	2007	2006	2007	2006
Release of deferred connection charges (Note 23)	927	924	927	924
Rental income	6,753	7,600	6,085	6,827
Domestic call revenue	13,846	13,902	9,469	10,745
Receipts from other network operators - domestic	419	244	563	356
International call revenue	2,068	2,237	1,760	2,033
Receipts from other network operators - international	287	109	259	339
International settlements (in payments)	7,146	5,940	7,146	5,940
CDMA revenue	6,188	5,520	6,188	5,520
Telex, data transmission and other telephony services	5,600	4,215	4,671	3,425
	<b>43,234</b>	<b>40,691</b>	<b>37,068</b>	<b>36,109</b>

In 2003, an organisation identifying itself as 'The Consumer Associations of Lanka' initiated legal action in the Court of Appeal seeking a writ of certiorari: to quash the approval granted by the Minister of Telecommunication and the Telecommunication Regulatory Commission of Sri Lanka for the tariff revisions implemented by the Company in September 2003.

The judgment delivered in July 2005 by the Court of Appeal granted the writ of certiorari quashing the approval granted for the tariff revision. The Company filed its application seeking special leave to appeal to the Supreme Court which was granted in November 2005.

As ordered by the Supreme Court on 27 August 2007 in respect of the judgment in the Case No 89/2005, the parties agreed on a settlement with a discount of 8.72% in the local call tariffs and rental charges effective from 1 January 2007. Accordingly, a credit amounting to Rs 1,394 million, which represents the excess charges made from 1 January 2007 to 31 October 2007, was refunded to customers with the November 2007 bills. This adjustment has been recognised as a reduction in revenue.

In terms of the same settlement, the revised tariffs from 1 November 2007 has been agreed at a discount of 9.03% of the previous tariffs. The revised tariffs have been incorporated into the time based billing (per second billing) structure adopted since 1 November 2007.

## NOTES TO THE FINANCIAL STATEMENTS

### 5. OPERATING COSTS

The following items have been included in arriving at operating profit:

	Group		Company	
	2007	2006	2007	2006
Staff costs (Note 6)	<b>6,090</b>	4,956	<b>5,479</b>	4,565
Directors' emoluments	<b>58</b>	31	<b>28</b>	29
Payments to international network operators	<b>1,454</b>	1,437	<b>1,454</b>	1,437
Payments to other network operators - international	<b>542</b>	451	<b>799</b>	681
Payments to other network operators - domestic	<b>511</b>	306	<b>393</b>	287
Auditors' remuneration				
Audit fees	<b>4</b>	4	<b>4</b>	3
Non-audit fees	<b>1</b>	-	<b>1</b>	-
Repairs and maintenance expenditure	<b>1,930</b>	1,754	<b>1,539</b>	1,478
Provision for doubtful debts	<b>1,191</b>	844	<b>1,036</b>	632
Provision for inventories	<b>(82)</b>	242	<b>(82)</b>	242
Net foreign exchange (gains)/losses	<b>(32)</b>	3	<b>(2)</b>	(43)
Other operating expenditure	<b>7,268</b>	5,587	<b>4,610</b>	3,686
CDMA expenditure	<b>1,813</b>	2,276	<b>1,972</b>	2,354
Write off of inventories	<b>-</b>	24	<b>-</b>	-
	<b>20,748</b>	17,915	<b>17,231</b>	15,351

### 6. STAFF COSTS

	Group		Company	
	2007	2006	2007	2006
Salaries, wages, allowances and other benefits	<b>5,155</b>	4,263	<b>4,621</b>	3,921
Retirement costs - defined contribution plans	<b>509</b>	407	<b>453</b>	370
- defined benefit obligations (Note 25)	<b>426</b>	286	<b>405</b>	274
	<b>6,090</b>	4,956	<b>5,479</b>	4,565
Average number of persons employed by the Group/Company during the year	<b>7,987</b>	7,980	<b>7,093</b>	7,241

### 7. INTERNATIONAL TELECOMMUNICATION OPERATORS' LEVY (ITL)

	Group		Company	
	2007	2006	2007	2006
Charge for the year	<b>2,851</b>	2,282	<b>2,727</b>	2,280

In terms of the Finance Act No. 11 of 2004, International Telecommunications Operators are required to make a contribution to the Government of Sri Lanka at the rate of US\$ 0.038 per international incoming traffic minute with effective from 3 March 2003. The total amount of the levy payable by the Company for the period from 1 January 2007 to 31 December 2007 was estimated at Rs. 2,727 million (2006 - Rs. 2,280 million) and has been recognised as an expense in the current financial year. The corresponding liability has been recognised in the balance sheet.

## NOTES TO THE FINANCIAL STATEMENTS

The Gazette notification No. 1386/24 of 31 March 2005 states that the levy will be credited as Incoming Local Access Charge (ILAC) and Telecommunications Development Charge (TDC) as per the rates specified in the Tables B and C to these regulations. These regulations also allow the domestic PSTN operators to claim two thirds of the TDC within three years against the cost of development of its telecommunications network in unserved and underserved areas of Sri Lanka as determined by the Telecommunications Regulatory Commission (TRC).

The documentation supporting the amount claimed from TDC against the cost of telecommunications network roll out in unserved and underserved areas by the Company has been submitted to the TRC. The estimated refund as at 31 December 2007 has not been recognised in the income statement pending approval by the TRC.

### 8. VOLUNTARY RETIREMENT SCHEME (VRS)

A VRS was announced on 30 April 2007. Accordingly, based on the number of applications received from employees, a VRS cost of Rs. 43 million was recognised in the income statement (2006 - Rs. 425 million).

### 9. INTEREST EXPENSE AND FINANCE COSTS

	Group		Company	
	2007	2006	2007	2006
<b>Interest expense and finance costs</b>				
Rupee loans	1,232	1,066	313	356
Foreign currency loans	75	135	35	89
US\$ 100 million notes	837	864	837	864
Other charges [Note (a)]	(17)	(109)	(17)	(109)
Total interest and finance costs	2,127	1,956	1,168	1,200
Interest capitalised	(90)	(140)	-	-
Net total interest and finance costs	2,037	1,816	1,168	1,200
Foreign exchange losses recognised from hedging reserve (Note 29)	195	68	195	68
Interest expenses and finance costs charged to income statement	2,232	1,884	1,363	1,268

(a) Other charges mainly include unrealised exchange gain of Rs. 117 million arising from revaluation of the fixed deposits in US\$ and unrealised exchange loss of Rs. 100 million arising from revaluation of the US\$ 100 million Bond.

### 10. INTEREST INCOME

	Group		Company	
	2007	2006	2007	2006
Interest income from - bank deposits	953	834	906	669
- financial assets	256	144	256	144
- related companies	-	-	-	295
- staff loans	77	58	77	58
	1,286	1,036	1,239	1,166

## NOTES TO THE FINANCIAL STATEMENTS

### 11. TAXATION

The charge for taxation is made up as follows:

	Group		Company	
	2007	2006	2007	2006
Income tax charge	4,495	5,289	4,479	5,232
Release of deferred tax liability (Note 22)	(1,736)	(1,500)	(1,736)	(1,500)
	<b>2,759</b>	3,789	<b>2,743</b>	3,732

The tax charge differs from the theoretical amount that would arise using the basic tax rate on the accounting profit of the Company and Group as follows:

	Group		Company	
	2007	2006	2007	2006
Profit before tax	8,399	9,227	8,131	9,229
Tax calculated at a tax rate of 33 1/3% (2006 - 33 1/3%)	2,799	3,076	2,710	3,076
Tax effect of income not subject to tax	(2,617)	(1,909)	(283)	(142)
Expenses not deductible for tax purposes	2,445	1,955	184	131
Effect of changes in tax rates	132	667	132	667
Tax charge	<b>2,759</b>	3,789	<b>2,743</b>	3,732

### 12. EARNINGS PER SHARE

The basic earnings per share is calculated by dividing the net profit attributable to equity holders by the weighted average number of ordinary shares in issue during the year.

	Group		Company	
	2007	2006	2007	2006
Net profit attributable to equity holders (Rs. million)	5,640	5,438	5,388	5,497
Weighted average number of ordinary shares in issue (million)	1,805	1,805	1,805	1,805
Basic earnings per share (Rs.)	<b>3.12</b>	3.01	<b>2.99</b>	3.05

### 13. DIVIDENDS

In respect of 2006, a first and final dividend of Rs. 1/- per share amounting to Rs. 1,804,860,000/- was paid during the current year and in respect of 2005, a first and final dividend of Rs. 0.75 per share amounting to a total of Rs. 1,353,645,000/- was paid during 2006.

The Board has recommended a first and final dividend of Rs. 1/- per share amounting to Rs. 1,804,860,000/- for the year ended 31 December 2007. This is to be approved by the shareholders at the Annual General Meeting to be held on 28 March 2008. As stipulated by Sri Lanka Accounting Standard No. 12 (Revised) - Events After the Balance Sheet Date, the proposed dividend is not recognised as a liability as at 31 December 2007.

## NOTES TO THE FINANCIAL STATEMENTS

### 14. PROPERTY, PLANT & EQUIPMENT

Group	Freehold land	Freehold buildings	Ducts, cables and other outside plant	Telephone exchanges	Transmission equipment	Other fixed assets	Capital work-in- progress	Total
<b>At 31 December 2005</b>								
Cost	333	1,649	66,008	17,996	24,828	8,674	3,288	122,776
Accumulated depreciation	–	(300)	(41,256)	(9,621)	(10,874)	(4,644)	–	(66,695)
<b>Net book amount</b>	<b>333</b>	<b>1,349</b>	<b>24,752</b>	<b>8,375</b>	<b>13,954</b>	<b>4,030</b>	<b>3,288</b>	<b>56,081</b>
<b>Year ended 31 December 2006</b>								
Opening net book amount	333	1,349	24,752	8,375	13,954	4,030	3,288	56,081
Additions at cost	–	–	128	13	415	1,098	6,857	8,511
Transfers from work-in-progress	4	312	2,569	534	2,551	197	(6,167)	–
Disposals at cost	–	–	–	–	(458)	(5)	–	(463)
Adjustments	–	(18)	31	(11)	(49)	35	–	(12)
Accumulated depreciation on disposal	–	–	–	–	44	5	–	49
Depreciation charge	–	(45)	(5,182)	(1,258)	(2,113)	(1,366)	–	(9,964)
<b>Closing net book amount</b>	<b>337</b>	<b>1,598</b>	<b>22,298</b>	<b>7,653</b>	<b>14,344</b>	<b>3,994</b>	<b>3,978</b>	<b>54,202</b>
<b>At 31 December 2006</b>								
Cost	337	1,943	68,736	18,532	27,287	9,988	3,978	130,801
Accumulated depreciation	–	(345)	(46,438)	(10,879)	(12,943)	(5,994)	–	(76,599)
<b>Net book amount</b>	<b>337</b>	<b>1,598</b>	<b>22,298</b>	<b>7,653</b>	<b>14,344</b>	<b>3,994</b>	<b>3,978</b>	<b>54,202</b>
<b>Year ended 31 December 2007</b>								
Opening net book amount	337	1,598	22,298	7,653	14,344	3,994	3,978	54,202
Additions at cost	–	–	176	16	986	1,896	6,861	9,935
Transfers from work-in-progress	10	290	1,170	214	3,799	191	(5,674)	–
Disposals at cost	–	–	–	–	(30)	(40)	–	(70)
Adjustments	–	(35)	2	–	(40)	70	–	(3)
Accumulated depreciation on disposal	–	–	–	–	8	29	–	37
Depreciation charge	–	(52)	(4,970)	(1,254)	(2,351)	(1,593)	–	(10,220)
<b>Closing net book amount</b>	<b>347</b>	<b>1,801</b>	<b>18,676</b>	<b>6,629</b>	<b>16,716</b>	<b>4,547</b>	<b>5,165</b>	<b>53,881</b>
<b>At 31 December 2007</b>								
Cost	347	2,197	70,084	18,762	32,002	12,105	5,165	140,662
Accumulated depreciation	–	(396)	(51,408)	(12,133)	(15,286)	(7,558)	–	(86,781)
<b>Net book amount</b>	<b>347</b>	<b>1,801</b>	<b>18,676</b>	<b>6,629</b>	<b>16,716</b>	<b>4,547</b>	<b>5,165</b>	<b>53,881</b>

## NOTES TO THE FINANCIAL STATEMENTS

Company	Freehold land	Freehold buildings	Ducts, cables and other outside plant	Telephone exchanges	Transmission equipment	Other fixed assets	Capital work-in- progress	Total
<b>At 31 December 2005</b>								
Cost	333	1,649	65,858	17,996	13,754	8,126	2,898	110,614
Accumulated depreciation	–	(300)	(41,124)	(9,621)	(7,747)	(4,285)	–	(63,077)
<b>Net book amount</b>	<b>333</b>	<b>1,349</b>	<b>24,734</b>	<b>8,375</b>	<b>6,007</b>	<b>3,841</b>	<b>2,898</b>	<b>47,537</b>
<b>Year ended 31 December 2006</b>								
Opening net book amount	333	1,349	24,734	8,375	6,007	3,841	2,898	47,537
Additions at cost	–	–	128	13	117	1,022	4,636	5,916
Transfers from work-in-progress	4	312	2,569	534	720	197	(4,336)	–
Disposals at cost	–	–	–	–	–	(5)	–	(5)
Adjustments	–	(18)	31	(11)	(49)	35	–	(12)
Accumulated depreciation on disposal	–	–	–	–	–	5	–	5
Depreciation charge	–	(45)	(5,132)	(1,257)	(1,065)	(1,309)	–	(8,808)
<b>Closing net book amount</b>	<b>337</b>	<b>1,598</b>	<b>22,330</b>	<b>7,654</b>	<b>5,730</b>	<b>3,786</b>	<b>3,198</b>	<b>44,633</b>
<b>At 31 December 2006</b>								
Cost	337	1,943	68,586	18,532	14,542	9,368	3,198	116,506
Accumulated depreciation	–	(345)	(46,256)	(10,878)	(8,812)	(5,582)	–	(71,873)
<b>Net book amount</b>	<b>337</b>	<b>1,598</b>	<b>22,330</b>	<b>7,654</b>	<b>5,730</b>	<b>3,786</b>	<b>3,198</b>	<b>44,633</b>
<b>Year ended 31 December 2007</b>								
Opening net book amount	337	1,598	22,330	7,654	5,730	3,786	3,198	44,633
Additions at cost	–	–	176	16	90	1,705	3,615	5,602
Transfers from work-in-progress	10	290	1,170	214	353	191	(2,228)	–
Disposals at cost	–	–	–	–	–	(17)	–	(17)
Adjustments	–	(35)	2	–	(40)	72	–	(1)
Accumulated depreciation on disposal	–	–	–	–	–	17	–	17
Depreciation charge	–	(52)	(4,970)	(1,254)	(1,119)	(1,489)	–	(8,884)
<b>Closing net book amount</b>	<b>347</b>	<b>1,801</b>	<b>18,708</b>	<b>6,630</b>	<b>5,014</b>	<b>4,265</b>	<b>4,585</b>	<b>41,350</b>
<b>At 31 December 2007</b>								
Cost	347	2,197	69,934	18,762	14,944	11,321	4,585	122,090
Accumulated depreciation	–	(396)	(51,226)	(12,132)	(9,930)	(7,056)	–	(80,740)
<b>Net book amount</b>	<b>347</b>	<b>1,801</b>	<b>18,708</b>	<b>6,630</b>	<b>5,014</b>	<b>4,265</b>	<b>4,585</b>	<b>41,350</b>

On 1 September 1991, the Department of Telecommunications (DOT) transferred its entire telecommunications business and related assets and liabilities to SLT. A valuation of the assets and liabilities transferred to SLT was performed by the Government of Sri Lanka. The net amount of those assets and liabilities represents SLT's Contributed Capital on incorporation, and the value of property, plant & equipment as determined by the Government of Sri Lanka valuers was used as the opening cost of fixed assets on 1 September 1991 in the first statutory accounts of SLT.

Further, SLT was converted into a public limited company, Sri Lanka Telecom Limited (SLTL), on 25 September 1996 and on that date, all of the business and the related assets and liabilities of SLT were transferred to SLTL as part of the privatisation process.

## NOTES TO THE FINANCIAL STATEMENTS

- (a) The cost of fully depreciated assets still in use as at 31 December 2007 was Rs. 22,545 million (2006 - Rs. 20,030 million).
- (b) No assets have been mortgaged or pledged as security for borrowings.
- (c) The Directors believe that the Company has freehold title to the land and buildings transferred on incorporation (Conversion of SLT into a public limited company on 25 September 1996), although the vesting orders specifying all the demarcations and extents of such land and buildings has not been formally issued.
- (d) The property, plant & equipment is not insured except for third party motor vehicle insurance. An insurance reserve has been created together with a sinking fund investment to meet any potential losses with regard to uninsured property, plant & equipment. At the balance sheet date, the insurance reserve amounted to Rs. 204 million (2006 - Rs. 183 million) (Note 26). The sinking fund investment is included under cash and cash equivalents [Note 20 (a)].
- (e) Additions include assets costing Rs. 33 million (2006 - Rs. 10 million) obtained under finance leases (where the Group/Company is the lessee).
- (f) The property, plant & equipment includes motor vehicles acquired under finance leases, the net book value of which is made up as follows:

	Group		Company	
	2007	2006	2007	2006
Cost	<b>43</b>	10	<b>43</b>	10
Accumulated depreciation	<b>(8)</b>	(3)	<b>(8)</b>	(3)
Net book amount	<b>35</b>	7	<b>35</b>	7

## NOTES TO THE FINANCIAL STATEMENTS

### 15. INTANGIBLE ASSETS

Group	Goodwill	Licences	Software	Others	Total
<b>At 1 January 2006</b>					
Cost	388	102	70	764	1,324
Accumulated amortisation and impairment	(247)	(20)	–	(375)	(642)
<b>Net book amount</b>	<b>141</b>	<b>82</b>	<b>70</b>	<b>389</b>	<b>682</b>
<b>Year ended 31 December 2006</b>					
Opening net book amount	141	82	70	389	682
Adjustments	–	–	(52)	–	(52)
Additions at cost	–	500	668	–	1,168
Amortisation charge	–	(57)	(41)	(112)	(210)
<b>Closing net book amount</b>	<b>141</b>	<b>525</b>	<b>645</b>	<b>277</b>	<b>1,588</b>
<b>At 31 December 2006</b>					
Cost	388	602	738	764	2,492
Accumulated amortisation and impairment	(247)	(77)	(93)	(487)	(904)
<b>Net book amount</b>	<b>141</b>	<b>525</b>	<b>645</b>	<b>277</b>	<b>1,588</b>
<b>Year ended 31 December 2007</b>					
Opening net book amount	141	525	645	277	1,588
Additions at cost	–	–	222	–	222
Amortisation charge	–	(14)	(112)	(70)	(196)
<b>Closing net book amount</b>	<b>141</b>	<b>511</b>	<b>755</b>	<b>207</b>	<b>1,614</b>
<b>At 31 December 2007</b>					
Cost	388	602	960	764	2,714
Accumulated amortisation and impairment	(247)	(91)	(205)	(557)	(1,100)
<b>Net book amount</b>	<b>141</b>	<b>511</b>	<b>755</b>	<b>207</b>	<b>1,614</b>

## NOTES TO THE FINANCIAL STATEMENTS

Company	Goodwill	Licences	Software	Others	Total
<b>At 1 January 2006</b>					
Cost	–	–	70	330	400
Accumulated amortisation and impairment	–	–	–	(246)	(246)
<b>Net book amount</b>	<b>–</b>	<b>–</b>	<b>70</b>	<b>84</b>	<b>154</b>
<b>Year ended 31 December 2006</b>					
Opening net book amount	–	–	70	84	154
Additions at cost	–	–	202	–	202
Adjustments	–	–	(7)	–	(7)
Amortisation charge	–	–	(42)	(47)	(89)
<b>Closing net book amount</b>	<b>–</b>	<b>–</b>	<b>223</b>	<b>37</b>	<b>260</b>
<b>At 31 December 2006</b>					
Cost	–	–	272	330	602
Accumulated amortisation and impairment	–	–	(49)	(293)	(342)
<b>Net book amount</b>	<b>–</b>	<b>–</b>	<b>223</b>	<b>37</b>	<b>260</b>
<b>Year ended 31 December 2007</b>					
Opening net book amount	–	–	223	37	260
Additions at cost	–	–	210	–	210
Amortisation charge	–	–	(64)	(30)	(94)
<b>Closing net book amount</b>	<b>–</b>	<b>–</b>	<b>369</b>	<b>7</b>	<b>376</b>
<b>At 31 December 2007</b>					
Cost	–	–	482	330	812
Accumulated amortisation and impairment	–	–	(113)	(323)	(436)
<b>Net book amount</b>	<b>–</b>	<b>–</b>	<b>369</b>	<b>7</b>	<b>376</b>

### Goodwill

As stated in Accounting Policy 2.6 (a), the Company has measured goodwill acquired in business combinations at cost less accumulated impairment losses. Such accounting policy has been prospectively applied with effect from 1 January 2006 in conformity with Revised SLAS 25 - Business Combinations.

### Others

As explained in Accounting Policy 2.6 (d), insurance premium paid by the Company to secure foreign loans under the 150K Project Scheme has been deferred on the basis that the benefit of this expenditure is not exhausted in the period in which it is incurred and will be written off to the income statement over a period of 10 years.

## NOTES TO THE FINANCIAL STATEMENTS

### 16. INVESTMENTS IN SUBSIDIARIES

	Company	
	2007	2006
Investment in subsidiary [Sri Lanka Telecom (Services) Limited] [Note (a)]	25	25
Investment in subsidiary [Mobitel (Private) Limited]		
<b>At 1 January</b>	<b>6,972</b>	3,472
Additions [Note (b)]	750	3,500
<b>At 31 December [Note (d)]</b>	<b>7,722</b>	6,972
Investment in subsidiary [SLT (Hong Kong) Limited] [Note (c)]		
<b>At 1 January</b>	<b>35</b>	-
Additions	-	35
<b>At 31 December</b>	<b>35</b>	35
Aggregate cost of investments at 31 December	<b>7,782</b>	7,032

- (a) This investment in subsidiary company consists of 2,500,000 shares representing a 100% holding of the issued share capital of Sri Lanka Telecom (Services) Limited.
- (b) Additions comprise the capital infusion of Rs. 750 million in 12% cumulative and redeemable preference shares of Mobitel (Private) Limited.
- (c) This investment in subsidiary company consists of 2,500,000 shares representing a 100% holding of the issued ordinary share capital of SLT (Hong Kong) Limited.
- (d) The Company owns 119,238,240 shares representing 100% of the issued ordinary share capital of Mobitel (Private) Limited. In addition, at 31 December 2007, the Company held 575,000,000 12% cumulative and redeemable preference shares of Mobitel (Private) Limited with a value of Rs. 10/- per share. The preference dividend rank above ordinary dividends.

At 31 December 2007, preference dividends amounting to Rs. 956 million were in arrears (31 December 2006 - Rs. 349 million). No accrual has been made in the Company's financial statements.

### 17. NON-CURRENT RECEIVABLES

	Group		Company	
	2007	2006	2007	2006
Employee loans [Note (a)]	1,268	960	1,268	960

- (a) Employee loans are repayable in equal monthly instalments over the loan period not exceeding six years. The amount shown as a non-current receivable represent staff loan instalments falling due after 1 January 2009.
- (b) The weighted average interest rates on staff loans are ranging from 3% to 7% (2006 - 3% to 7%).

## NOTES TO THE FINANCIAL STATEMENTS

### 18. INVENTORIES

Inventories consist of engineering stores, consumables, office equipment and hardware, and is stated net of provisions for slow-moving and obsolete items.

### 19. RECEIVABLES AND PREPAYMENTS

	Group		Company	
	2007	2006	2007	2006
Domestic trade receivables	6,870	7,393	6,011	6,723
CDMA instalment debtors	340	709	340	709
Foreign trade receivables	1,386	1,251	1,386	1,251
Amount due from related parties [Note 33 (e)]	-	-	1,650	1,165
Advances and prepayments [Note (a)]	212	164	144	120
Employee loans	324	333	324	333
Other receivables [Note (b)]	806	708	209	253
<b>Amounts due within one year</b>	<b>9,938</b>	<b>10,558</b>	<b>10,064</b>	<b>10,554</b>

(a) Advances and prepayments of the Company mainly consist of advances on purchases Rs. 89 million (2006 - Rs. 28 million) and payments for software maintenance Rs. 37 million (2006 - Rs. 75 million).

(b) Other receivables of the Company mainly consist of interest receivable of Rs. 165 million (2006 - Rs. 212 million) refundable deposits of Rs. 42 million (2006 - Rs. 30 million) and dishonored cheques of Rs. 2 million (2006 - Rs. 10 million). In addition, other receivables of the Group include VAT receivable of Rs. 428 million (2006 - Rs. 367 million) of Mobitel (Private) Limited.

### 20. CASH AND CASH EQUIVALENTS

	Group		Company	
	2007	2006	2007	2006
Cash at bank and in hand	393	279	79	159
Restricted at bank [Note (a)]	7,244	4,608	7,244	4,608
Short-term deposits [Note (b)]	9,558	10,428	9,366	9,623
	<b>17,195</b>	<b>15,315</b>	<b>16,689</b>	<b>14,390</b>

(a) The restricted cash balance represents a deposit of Sri Lankan Rupees 204 million (2006 - Rs. 183 million) at People's Bank of Sri Lanka representing the sinking fund investment for the insurance reserve and a sinking fund amounting to Rs. 7,039 million (2006 - Rs. 4,426 million) maintained to redeem the US\$ 100 million Bond in 2009. The restrictions on these balances are self-imposed.

(b) The interest on short-term bank deposits are on commercial terms. The weighted average effective interest rate on short-term LKR and US\$ bank deposits was 15.9% (2006 - 10.43%) and 5.89% (2006 - 5.39%) respectively.

## NOTES TO THE FINANCIAL STATEMENTS

(c) For the purpose of the cash flow statement, the year-end cash and cash equivalents comprise the following:

	Group		Company	
	2007	2006	2007	2006
Cash and cash equivalents	17,195	15,315	16,689	14,390
Bank overdrafts (Note 21)	(275)	(980)	-	-
	<b>16,920</b>	14,335	<b>16,689</b>	14,390

### 21. BORROWINGS

	Group		Company	
	2007	2006	2007	2006
<b>Current (due within one year)</b>				
Bank overdrafts (Note 20)	275	980	-	-
Government borrowings	696	678	696	678
Bank borrowings and others	1,646	2,257	129	774
Lease liabilities	8	2	8	2
	<b>2,625</b>	3,917	<b>833</b>	1,454
<b>Non-current (due after one year)</b>				
Government borrowings	1,299	1,994	1,299	1,994
Bank borrowings and others	4,405	4,041	111	238
US\$ 100 million Notes	10,925	10,825	10,925	10,825
Lease liabilities	31	8	31	8
	<b>16,660</b>	16,868	<b>12,366</b>	13,065
<b>Total borrowings</b>	<b>19,285</b>	20,785	<b>13,199</b>	14,519

(a) The interest rate exposure of the borrowings of the Group and Company were as follows:

	Group		Company	
	2007	2006	2007	2006
<b>Total borrowings</b>				
- at fixed rates	11,481	11,851	11,206	11,851
- at floating rates	7,804	8,934	1,993	2,668
	<b>19,285</b>	20,785	<b>13,199</b>	14,519

## NOTES TO THE FINANCIAL STATEMENTS

The current exposure of the borrowings of the Group and Company at the balance sheet date was as follows:

	Group		Company	
	2007	2006	2007	2006
Foreign currency	<b>11,687</b>	12,565	<b>11,165</b>	11,837
Local currency	<b>7,598</b>	8,220	<b>2,034</b>	2,682
	<b>19,285</b>	20,785	<b>13,199</b>	14,519

	Group/Company	
	2007	2006
Average effective interest rates:		
- Bank overdrafts	<b>16.29%</b>	13.41%
- Foreign bank borrowings	<b>5.31%</b>	5.21%
- Government borrowings	<b>12.21%</b>	11.10%
- US\$ 100 million Notes	<b>6.875%</b>	6.875%

Maturity of non current borrowings:

	Group		Company	
	2007	2006	2007	2006
Between 1 and 2 years	<b>13,523</b>	13,839	<b>12,344</b>	12,415
Between 3 and 5 years	<b>3,137</b>	3,029	<b>22</b>	650
	<b>16,660</b>	16,868	<b>12,366</b>	13,065

Finance lease liabilities - minimum lease payments

	Group		Company	
	2007	2006	2007	2006
Not later than 1 year	<b>13</b>	3	<b>13</b>	3
Later than 1 year and not later than 5 years	<b>44</b>	11	<b>44</b>	11
	<b>57</b>	14	<b>57</b>	14
Less: future finance charges on finance leases	<b>(18)</b>	(4)	<b>(18)</b>	(4)
Present value of finance lease liabilities	<b>39</b>	10	<b>39</b>	10

Representing lease liabilities

	Group		Company	
	2007	2006	2007	2006
Current	<b>8</b>	2	<b>8</b>	2
Non-current	<b>31</b>	8	<b>31</b>	8
	<b>39</b>	10	<b>39</b>	10

## NOTES TO THE FINANCIAL STATEMENTS

- (b) The Government of Sri Lanka had borrowed amounts in foreign currencies to fund the development of the Company's telecommunication network. These amounts had been re-lent to the Company with shorter repayment periods than the underlying loan. The total borrowings of Government of Sri Lanka as at 31 December 2007 was Rs. 1,995 million (2006 - Rs. 2,672 million). The exchange fluctuations of these loans are borne by the Government of Sri Lanka.
- (c) The Government of Sri Lanka has guaranteed third party loans of the Company amounting to Rs. 240 million (2006 - Rs. 1,012 million). Total value of borrowings that have neither been guaranteed nor secured by the Government of Sri Lanka is Rs. 10,925 million (2006 - Rs. 10,825 million).
- (d) The loan covenants include submission of audited financial statements to the lenders within specified periods from the financial year end, and to maintain adequate accounting records in accordance with generally accepted accounting principles.
- (e) The Directors believe that the Company will have sufficient fund available to meet its present loan commitments.

### 22. DEFERRED INCOME TAXES

Deferred income taxes are calculated on all temporary differences arising from difference between accounting base and tax base. Deferred income tax is provided under the liability method using a principal tax rate of 35% which will be effective from year of assessment 2008/09 (year of assessment 2007/08 - 33 1/3%).

The movement in the deferred income tax account is as follows:

	Group		Company	
	2007	2006	2007	2006
At beginning of the year	4,513	6,013	4,513	6,013
Income statement release (Note 11)	(1,736)	(1,500)	(1,736)	(1,500)
<b>At end of year</b>	<b>2,777</b>	4,513	<b>2,777</b>	4,513

The temporary differences mainly arise from property, plant & equipment and, provision for gratuity.

### 23. DEFERRED INCOME

Deferred income represents the connection charges relating to PSTN network, net of amounts amortised to the income statement. The connection charges are amortised over a period of 15 years as stated in Accounting Policy 2.21 (iv).

The movement in the deferred income is as follows:

	Group/Company	
	2007	2006
At beginning of year	7,110	7,546
Connection fees for the year	246	488
Amount credited to income statement during the year (Note 4)	(927)	(924)
<b>At end of year</b>	<b>6,429</b>	7,110

## NOTES TO THE FINANCIAL STATEMENTS

### 24. TRADE AND OTHER PAYABLES

	Group		Company	
	2007	2006	2007	2006
<b>Amounts due within one year</b>				
Domestic trade payables	1,321	921	85	103
Foreign trade payables	157	292	157	292
Amount due to related parties [Note 33 (e)]	-	-	357	158
Capital expenditure payables [Note (a)]	2,327	1,656	1,083	1,319
Deferred revenue	235	181	-	-
Social security and other taxes [Note (b)]	361	407	361	407
Interest payable	138	148	138	148
Other payables [Note (c)]	6,870	5,116	6,356	4,903
	<b>11,409</b>	8,721	<b>8,537</b>	7,330
<b>Amounts due after one year</b>				
International Direct Dialling deposits	235	233	235	233
Prepayments on VOIP services	44	65	44	65
	<b>279</b>	298	<b>279</b>	298

- (a) Capital expenditure payables of the Company mainly consist of contractors' payables Rs. 297 million (2006 - Rs. 626 million) and advances on network restoration after road works of Rs. 577 million (2006 - Rs. 513 million).
- (b) Social security and other taxes of the Company mainly consist of Value Added Tax Rs. 223 million (2006 - Rs. 267 million).
- (c) Other payables of the Company mainly consist of Rs. 244 million (2006 - Rs. 244 million) dividend payable to Government of Sri Lanka, Rs. 105 million (2006 - 109 million) provision for Goods Received Notes (GRNs), Rs. 5,009 million (2006 - Rs. 3,475 million) International Telecommunication Operators' Levy and Rs. 152 million Cess (2006 - Rs. 165 million) payable to Director-General of Telecommunications.

### 25. RETIREMENT BENEFIT OBLIGATIONS

Movement in the liability recognised in the balance sheet is as follows:

	Group		Company	
	2007	2006	2007	2006
At beginning of the year	942	751	903	721
Current service cost (Note 6)	426	286	405	274
Amount due within a year transferred to other payables	-	(30)	-	(30)
Provision made for gratuity payable to VRS employees	30	-	30	-
<b>Contributions paid</b>				
- VRS employees	(38)	(42)	(38)	(42)
- Other employees	(31)	(23)	(28)	(20)
<b>At end of year</b>	<b>1,329</b>	942	<b>1,272</b>	903

- (a) As stated in Accounting Policy 2.19 (b) as at 31 December 2007, an actuarial valuation was carried out by an independent actuary.

## NOTES TO THE FINANCIAL STATEMENTS

The principal actuarial assumptions used were as follows:

	Company	
	2007	2006
Discount rate (long-term)	10%	10%
Future salary increases	9%	9%
Inflation rate (long-term)	10%	10%

In addition to the above, demographic assumptions such as mortality, withdrawal, retirement age were considered for the actuarial valuation. In 2007, 1967/70 Mortality Table issued by the Institute of Actuaries - London (2006 - 1967/70 Mortality Table) was taken as the base for the valuation.

### 26. INSURANCE RESERVE

	Group/Company	
	2007	2006
At beginning of the year	183	166
Income statement charge (deposit) and interest income on sinking fund deposit	21	17
At end of year	204	183

### 27. GROUP REPORTING DATES

The annual financial statements of the wholly owned subsidiaries, Sri Lanka Telecom (Services) Limited, SLT (Hong Kong) Limited, SLT Publications (Private) Limited and Mobitel (Private) Limited are prepared at 31 December each year.

### 28. STATED CAPITAL

	Company	
	2007	2006
<b>Issued and fully paid</b>		
1,804,860,000 ordinary shares issued at Rs. 10 per share	18,049	18,049

The issued and fully paid share capital is made up as follows:

	2007		2006	
	Holding %	No. of Shares	Holding %	No. of Shares
Government of Sri Lanka (GOSL)	49.50	893,405,700	49.50	893,405,700
NTT Communications Corporation (NTT Com)	35.20	635,076,318	35.20	635,076,318
Employees and the public	15.30	276,377,982	15.30	276,377,982
	<b>1,804,860,000</b>		<b>1,804,860,000</b>	

## NOTES TO THE FINANCIAL STATEMENTS

### 29. HEDGING RESERVE

	Group/Company	
	2007	2006
At beginning of the year	(236)	(208)
- Foreign currency translation difference	(17)	(96)
- Income statement charge (Note 9)	195	68
<b>At end of year</b>	<b>(58)</b>	<b>(236)</b>

In terms of the risk management objectives, the Company hedged certain foreign currency borrowings against its foreign currency revenue streams. The future transactions are forecast for a period of five years. The gains/(losses) from revaluation of these foreign currency loans are deferred to be matched against the gains/(losses) from the future revenue streams.

### 30. CASH GENERATED FROM OPERATIONS

Reconciliation of profit before tax to cash generated from operations

	Group		Company	
	2007	2006	2007	2006
Profit before tax	8,399	9,227	8,131	9,229
<b>Adjustments for</b>				
Depreciation (Note 14)	10,220	9,964	8,884	8,808
Amortisation of grants	(7)	(14)	(7)	(14)
Amortisation of intangible assets (Note 15)	196	210	94	89
Interest expense and finance costs (Note 9)	2,232	1,884	1,363	1,268
Interest income (Note 10)	(1,286)	(1,036)	(1,239)	(1,166)
Connection fees less amortisation (Note 23)	(681)	(436)	(681)	(436)
Profit on sale of property, plant & equipment	(15)	(4)	(15)	(4)
Provision for insurance reserve net of interest income (Note 26)	21	17	21	17
Retirement benefit obligations	387	221	369	212
Write off of inventories	-	24	-	-
	<b>19,466</b>	<b>20,057</b>	<b>16,920</b>	<b>18,003</b>
<b>Changes in working capital</b>				
- receivables and prepayments	(86)	(1,625)	(216)	(2,245)
- inventories	(57)	(551)	(48)	(631)
- payables	2,680	1,456	1,198	1,121
Cash generated from operations	<b>22,003</b>	<b>19,337</b>	<b>17,854</b>	<b>16,248</b>

### 31. COMMITMENTS

#### Capital commitments

The Group/Company has purchased commitments in the ordinary course of business as at 31 December 2007 as follows:

	Group		Company	
	2007	2006	2007	2006
Property, plant & equipment				
- approved but not contracted	9,888	7,295	9,888	7,295
- approved and contracted	6,707	4,217	3,077	2,484
	<b>16,595</b>	<b>11,512</b>	<b>12,965</b>	<b>9,779</b>

## NOTES TO THE FINANCIAL STATEMENTS

### Operating lease commitments

The future minimum lease payments under operating leases are as follows:

	Group		Company	
	2007	2006	2007	2006
Later than one year and not later than five years	173	244	173	244

### Other financial commitments

Except for any regular maintenance contracts entered into with third parties in the normal course of business, there are no other material financial commitments that requires separate disclosure.

## 32. CONTINGENCIES

- (a) An arbitration proceeding was initiated under ICC Arbitration application No.13839/M by Informatics (Pvt) Limited, claiming US\$ 1,143,630 being the licence upgrade cost and an annual maintenance fee of 15% of the licence fee for the TBR system provided to SLTPLC by Informatics.
- (b) Global Electroteks Limited has initiated legal action under High Court Case No. 20/2005 claiming damages of US\$ 12 million from SLTPLC for unlawful disconnection of interconnection services.
- (c) SLTPLC has filed a revision application in High Court, Anuradhapura to set aside an order given by Magistrate to hand over the vacant possession of the property at Niwanthaka Chethiya Road, Anuradhapura.
- (d) Under Court of Appeal CA No. 883/2003 SLTPLC is seeking a writ of certiorari to quash the award given by the Arbitrator at the Labour Arbitration, increasing the overtime rate from 1.5% to 1.75% and granting of lieu leave with regard to an application made by the Telecommunications Employees' Union with effect from 1 February 1998.
- (e) Directories Lanka (Private) Limited (DLPL) filed case No. 2/2006 (3) in Commercial High Court against SLTPLC claiming Rs. 250 million, damages for unfair competition with regard to Artwork on the cover page of SLT Directory Publication.
- (f) With regard to cases detailed under (a), (b), (c), (d) and (e) above, pending the outcome of the appeal, no adjustment has been made in the financial statements up to 31 December 2007.
- (g) In addition to the above referred cases, there are more litigation issues in relation to claims by employees and third parties for damages. In the opinion of the Directors none of these actions are likely to result a material liability to the Company.

## NOTES TO THE FINANCIAL STATEMENTS

### 33. DIRECTORS' INTERESTS IN CONTRACTS

- (a) A Director is considered to have a direct interest in a contract with the Company, if the Director himself/herself is involved in a contract with the Company. A Director has an indirect interest in a contract with the Company, if the Director, through his/her common Directorships or his/her dependent family members is involved in a contract with the Company.

The Directors of Sri Lanka Telecom PLC held directorship in the following entities during the year:

Director	Company	Position
Mr. Shoji Takahashi	Mobitel (Private) Limited	Director
	SLT Publications (Private) Limited	Director
	Sri Lanka Telecom (Services) Limited	Director
	SLT (Hong Kong) Limited	Director
Mr. Shuhei Anan	Mobitel (Private) Limited	Director
Mr. P. Asoka Weerasinghe de Silva	Mobitel (Private) Limited	Chairman/Director
	SLT (Hong Kong) Limited	Chairman/Director
	SLT Publications (Private) Limited	Director
	Sri Lanka Telecom (Services) Limited	Director
Mrs. Leisha Chandrasena	Mobitel (Private) Limited	Director
	SLT (Hong Kong) Limited	Director
Mr. Sumith Wijesinghe	Mobitel (Private) Limited	Director
	National Development Trust (Guarantee) Limited	Director
	National Development Trust Fund	Trustee
Mr. Jun Sawada	NTT America, Inc.	Director
	Verio, Inc.	Director
	NTT Europe Limited	Director
	NTT Singapore Pte. Limited	Director
	NTT Communications China Co. Limited	Director
	NTT Worldwide Telecommunications Corporation	Director
Mr. S.N. Kumar	Milletechno, Inc	Director
	Mobitel (Private) Limited	Director

## NOTES TO THE FINANCIAL STATEMENTS

The Company had following transactions with related entities during the year under review:

	Company	
	2007	2006
<b>(b) Mobitel (Private) Limited</b>		
<b>Sale of goods and services:</b>		
Provision of E1 links	332	350
Interconnection charges	234	198
VOIP Platform	9	-
	575	548
<b>Purchase of goods and services:</b>		
Call charges relating to cellular phones purchased by the Company employees	44	32
Interconnection charges	167	144
Antenna tower space	159	78
	370	254

Number of new GSM connections granted (special packages with no monthly rental) in 2007 is 1,754 (2006 - 1,209).

The Company has provided the following guarantees on behalf of Mobitel (Private) Limited:

- (i) Loans amounting to Rs. 10,225 million (2006 - Rs. 6,496 million) and US\$ 4.8 million (2006 - US\$ 6.7 million) for GSM roll out stage 1 and 3 and operational expenses.
- (ii) A commitment guarantees amounting to Rs. 250 million (2006 - Rs. 250 million) issued by banks in favour of TRC for the purpose of 3G rollout.

**(c) NTT Communications Corporation**

As per the shareholders' agreement with NTT Com, the following charges have been borne by the Company:

	Company	
	2007	2006
<b>Purchase of goods and services:</b>		
Fees for secondment of personnel from NTT Com	43	48
Expenditure for personnel from NTT Com	11	6
	54	54
<b>(d) SLT (Hong Kong) Limited</b>		
<b>Sale of goods and services:</b>		
Leased circuits	4	-
<b>Purchase of goods and services:</b>		
Leased circuits	5	-

## NOTES TO THE FINANCIAL STATEMENTS

		Company	
		2007	2006
<b>(e)</b>	<b>Outstanding balances arising from sale/purchase of services above</b>		
	<b>Receivable from subsidiaries:</b>		
	Mobitel (Private) Limited	1,646	1,165
	SLT (Hong Kong) Limited	4	-
		<b>1,650</b>	<b>1,165</b>
	<b>Payable to subsidiaries:</b>		
	Mobitel (Private) Limited	350	152
	Sri Lanka Telecom (Services) Limited	2	6
	SLT (Hong Kong) Limited	5	-
		<b>357</b>	<b>158</b>

		Group		Company	
		2007	2006	2007	2006
<b>(f)</b>	<b>Key management compensation:</b>				
	Salaries and other benefits	70	47	52	31

### 34. RELATED PARTY RELATIONSHIPS AND TRANSACTIONS

Parties are considered to be related if one party has the ability to control the other party or exercise significant influence over the other party in making financial and operating decisions. A related party transaction takes place with a transfer of resources or obligations between related parties, regardless of whether a price is charged.

Sri Lanka Telecom (Services) Limited, is a related party of the Company. All transactions during the year and balances as at the balance sheet date between the two companies have been eliminated in preparing consolidated financial statements.

Mobitel (Private) Limited, is a related party of the Company. All transactions during the year and balances as at the balance sheet date between the two companies have been eliminated in preparing consolidated financial statements.

SLT Hong Kong Limited, is a related party of the Company. All transaction during the year and balances as at the Balance Sheet date between the two Companies have been eliminated in preparing consolidated financial statements.

SLT Publications (Private) Limited, is a related party of the Company. No transactions have occurred during the year between the two companies.

Related party transactions disclosed above should be read in conjunction with Note 33 to the financial statements.

### 35. POST-BALANCE SHEET EVENTS

No events have arisen since the balance sheet date which would require adjustments to, or disclosure in the financial statements.