

July 30, 2015

LEGAL ALERT

ComDer Central Counterparty S.A. Becomes Operational

On Thursday, July 30th, 2015, ComDer Central Counterparty S.A. began its operations, with the objective to manage netting and settlement of financial instruments.

To date, each bank typically performed derivatives transactions with customers or other banks on a bilateral basis; however, after the financial crisis of 2008, this became one of the most questionable practices. The laws regarding this matter began to be amended around the globe, and Chile wasn't an exception. In this context, law 20,345 was enacted on June 6th, 2009, and gave the legal framework for the Financial Instruments Netting and Settlement Systems, but it wasn't until this year that this law took capital importance, due to the creation of the Netting and Settlement Systems for OTC Derivative Instruments, known as COMDER CENTRAL COUNTERPARTY S.A. (ComDer).

ComDer is a company incorporated in accordance with Title II of Law 20,345, to manage netting and settlement of financial instruments, and that will act as a Central Counterparty. A Central Counterparty is the entity with which all operations that would otherwise be settled directly between the parties are settled on a multilateral basis. This system includes a Registration and Confirmation of Operations module and Repository Centralized Operations module. The Central Counterparty acts as a buyer for every seller and as a seller for every buyer, assuming each transaction payment liability and diminishing the bilateral direct interconnection between the institutions involved.

The shareholders of this entity are Servicios de Infraestructura de Mercado OTC S.A. and the Association of Banks and Financial Institutions of Chile AG. ComDer's direct participants are 17 banks and it has an investment portfolio in highly liquid financial instruments. In this sense, ComDer limits its market risk exposure by investing their surpluses in documents issued by the Central Bank, or fixed income financial instruments issued by banks and financial institutions, or fixed income mutual funds. Investments in financial instruments are short term. The financing policy gives preference to acting with ComDer's

own resources.

ComDer will operate by high security electronic means for reception, confirmation, acceptance, netting and settlement of compensation orders received from participants. Specifically, the buyer and seller encapsulate a message through the SWIFT global network, then ComDer matches the information and confirms that the transaction is correct. Once confirmed, the novation of the contract is made by the House, which requests the guarantees and makes the corresponding margin calls. The acceptance and compensation process is made in real-time and ComDer counterpart will always be a bank. The Central Counterparty objective is to avoid the system's default, which is accomplished by requesting guarantees from the participants. If one of them is not able to comply with its obligations, the Central Counterparty takes the administration of its portfolio and its guarantees, managing the positions.

Among the main benefits attributed to this new system are the increase in transparency and security in derivatives markets, a better balance between risk management and liquidity cost, operational efficiency improvements and, of course, reduced systemic risk. In addition, when transferring the operational risks to ComDer, the banks are releasing lines and capital requirements.

Finally, on July 23rd, 2015, ComDer received Exempt Resolution No. 226 issued by the Chilean Superintendency of Securities and Insurances, which gave the necessary authorization to initiate its activities, completing the final stage prior to its operation.

Under this authorization, the board of ComDer set as the starting date of operations Thursday, July 30th, 2015 as stated in the plan of implementation. With this commissioning, one of the items of the global regulatory agenda of the Chilean Central Bank was met.

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