

# International **Comparative** Legal Guides



## Derivatives **2020**

A practical cross-border insight into derivatives

**First Edition**

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# Chile



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## 1 Documentation and Formalities

**1.1 Please provide an overview of the documentation (or framework of documentation) on which derivatives transactions are typically entered into in your jurisdiction. If the 1992 or 2002 ISDA Master Agreements are not typically used, please describe the contracts which are used, as well as any appendices or annexures.**

Although Chilean law does not require any specific documentation for the valid execution of derivatives transactions, the 1992 ISDA Master Agreement, in its forms “Local Currency – Single Jurisdiction” and “Multicurrency – Cross Border”, and the 2002 ISDA Master Agreements, are typically used in our jurisdiction to enter into international derivatives transactions. For local derivatives transactions involving Chilean banks, the typical documentation is the Master Agreement for Derivatives Agreements in the Local Market (*Condiciones Generales para Contratos de Derivados en el Mercado Local*) approved by the Chilean Banking Association (*Asociación de Bancos e Instituciones Financieras*). These agreements have been recognised by the Central Bank of Chile (*Banco Central de Chile*) (the “**Central Bank**”) for the purposes of close-out netting of derivatives transactions (see section 5 below).

**1.2 Are there any variances in documentation for certain types of derivatives transactions or between certain types of counterparties in your jurisdiction? For example, what differences do you see between over-the-counter (“OTC”) and exchange-traded derivatives (“ETD”) or for particular asset classes?**

Unless the derivative contract is executed with a foreign counterparty, derivatives contracts in Chile are typically executed according to the Master Agreement for Derivatives Agreements in the Local Market referred to in question 1.1 above.

**1.3 Are there any particular documentary or execution requirements in your jurisdiction? For example, requirements as to notaries, number of signatories, or corporate authorisations?**

Pursuant to Chilean law, except for specific derivatives

transactions entered into by some regulated entities which must be evidenced in writing, no documentary nor execution requirements are needed to ensure that a derivative transaction is validly executed. However, not by reason of the formation of the agreement between the parties but by reason of proof of the existence of the same, it is recommendable to evidence in writing any transaction agreed over the telephone or by electronic means. In this regard, derivatives contracts executed by individuals or legal entities using an electronic signature will be valid in the same way and will produce the same effects as those executed in writing.

Regarding derivatives transactions entered into by legal entities located in Chile – and particularly with respect to those entered by regulated entities and institutional investors (e.g. banks, insurance companies, national reinsurance entities, etc.) – careful review of their bylaws and/or internal regulations should be made before executing the respective derivative contract since, in the case that corporate authorisation is needed, the omission thereof may cause the derivative transaction to be null and void under Chilean law.

**1.4 Which governing law is most often specified in ISDA documentation in your jurisdiction? Will the courts in your jurisdiction give effect to any choice of foreign law in the parties’ derivatives documentation? If the parties do not specify a choice of law in their derivatives contracts, what are the main principles in your jurisdiction that will determine the governing law of the contract?**

New York law and English law are often specified as governing law in ISDA documentation executed in our jurisdiction, with the former being more frequently used.

Under Chilean law, parties may freely and validly agree to the governing law of the derivative documentation and the courts will give effect to any choice of foreign law. If the parties do not specify a choice of law in their derivatives contracts, the governing law will be determined pursuant to conflict of laws’ rules applicable in Chile which state that the formalities of the contract are determined by the law of the jurisdiction in which it was executed, but if such contract is intended to be performed or to produce effects in Chile, such effects must conform to the requirements of Chilean law.

## 2 Credit Support

### 2.1 What forms of credit support are typically provided for derivatives transactions in your jurisdiction?

In the case of ISDA transactions, the forms commonly used are the 1994 and 1995 Credit Support Annexes (New York law).

### 2.2 How is credit support for derivatives transactions typically documented in your jurisdiction? For example, under an ISDA Credit Support Annex or Credit Support Deed.

Typically, credit support for ISDA derivatives transactions is documented under an ISDA Credit Support Annex. For local derivatives transactions, credit support is typically documented by each local bank credit support annex and through a Chilean law security (e.g., pledge).

### 2.3 Where transactions are collateralised, would this typically be by way of title transfer, by way of security, or a mixture of both methods?

Chilean law does not recognise – other than in a few exceptional cases, such as REPOs transactions – a transfer of title as valid security. Thus, where transactions are collateralised by an eligible credit support located onshore, this would typically be by way of security. An exception would be the pledge over cash. In this case, the pledge has a similar effect to a transfer of title: the collateral taker would be able to use, enjoy and dispose of the pledged money with the requirement to return an equivalent sum of money once the secured obligation is discharged.

### 2.4 What types of assets are acceptable in your jurisdiction as credit support for obligations under derivatives documentation?

Generally, both tangible (i.e., cash) and intangible (i.e., securities investments) movable assets are typically accepted as credit support for obligations under derivatives documentation.

### 2.5 Are there specific margining requirements in your jurisdiction to collateralise all or certain classes of derivatives transactions? For example, are there requirements as to the posting of initial margin or variation margin between counterparties?

There are no specific margining requirements in our jurisdiction to collateralise all or certain classes of derivatives transactions. Thus, parties may freely negotiate and agree the posting of initial or variation margins.

### 2.6 Does your jurisdiction recognise the role of an agent or trustee to enter into relevant agreements or appropriate collateral/enforce security (as applicable)? Does your jurisdiction recognise trusts?

Yes, the role of an agent is recognised under Article 18 of law No. 20,190 which created the legal concept of the collateral or security agent which, among other duties, can act as a trustee of the collateral given as security and has the authority to enforce rights against the collateral in the event of default.

### 2.7 What are the required formalities to create and/or perfect a valid security over an asset? Are there any regulatory or similar consents required with respect to the enforcement of security?

Chilean law allows the creation of security interests over all kinds of assets but the type of collateral in which a party is taking a security interest will dictate the formalities (regulated under different bodies of law) for perfecting the security interest.

Whilst no consents are required with respect to enforcement of securities, it is important to bear in mind that Chilean law does not allow self-help remedies and out-of-court enforcement of securities but provides for specific enforcement rules which are part of Chilean public policy and as such cannot be waived or contracted-out.

## 3 Regulatory Issues

### 3.1 Please provide an overview of the key derivatives regulation(s) applicable in your jurisdiction and the regulatory authorities with principal oversight.

There is no single or overarching law regulating derivatives in Chile. The main regulations include the following: Law No. 20,544 on Tax Treatment of Derivatives (the “Derivatives Taxation Law”); Chapter III.D of the Compendium of Financial Regulations of the Central Bank regarding derivatives transactions carried out in the local market; Chapter IX of the Foreign Exchange Regulations of the Central Bank – which basically imposes the obligation to comply with certain reporting requirements; and law No. 20,720 on Insolvency and Re-entrepreneurship (the “Chilean Insolvency Law”). Additionally, specific provisions concerning derivatives transactions are included in different regulations governing Chilean regulated entities and institutional investors.

Regulatory authorities with principal oversight will vary depending on the relevant entity entering into a derivative transaction: the Chilean Securities Market Commission (*Comisión para el Mercado Financiero*) supervises listed corporations, investment and mutual funds administrators, insurance and reinsurance companies, banks, investment firms and broker dealers, and the Pensions Commission (*Superintendencia de Pensiones*) oversees pension funds administrators. Also, the Central Bank, as the entity responsible for overseeing the stability of Chile’s currency and the proper operation of internal and external payments, has the authority to issue specific regulations applicable to derivatives transactions and to impose the obligation to comply with certain reporting requirements.

### 3.2 Are there any regulatory changes anticipated, or incoming, in your jurisdiction that are likely to have an impact on entry into derivatives transactions and/or counterparties to derivatives transactions? If so, what are these key changes and their timeline for implementation?

An anticipated regulatory change that is likely to have an impact on entry into derivatives transactions is the entry into force of Chapters III.D.3 and III.D.3.1 of the Compendium of Financial Regulations of the Central Bank. These regulations contemplate a new Integrated Information System on Derivatives Transactions and its Operational Regulation, a centralised electronic registry of derivatives transactions created to increase transparency, promote financial stability and prevent market abuses. These chapters will come into force on November 3, 2020 (please refer to question 8.3 below for additional details).

**3.3 Are there any further practical or regulatory requirements for counterparties wishing to enter into derivatives transactions in your jurisdiction? For example, obtaining and/or maintaining certain licences, consents or authorisations (governmental, regulatory, shareholder or otherwise) or the delegating of certain regulatory responsibilities to an entity with broader regulatory permissions.**

Practical or regulatory requirements vary depending on the type or nature of the Chilean counterparty, since applicable regulations, bylaws or internal policies may provide for limitations related to the type of derivative transaction, underlying asset or purpose (hedge or speculative), among others. For example, the Republic of Chile and the services and institutions of the public sector require a specific resolution from the Ministry of Finance to enter into a hedge transaction. Likewise, State-owned companies and companies majority-owned by the State require prior authorisation from the Ministry of Finance and the Ministry of Economy, Development and Tourism, by means of a joint Supreme Decree, if it is considered that the derivative transaction may affect the public credit, or an authorisation (general or specific) from the Ministry of Finance in all other cases.

**3.4 Does your jurisdiction provide any exemptions from regulatory requirements and/or for special treatment for certain types of counterparties (such as pension funds or public bodies)?**

There are no general exemptions from regulatory requirements and, as previously mentioned, different regulations apply to derivatives transactions made by regulated entities and institutional investors.

## 4 Insolvency/Bankruptcy

**4.1 In what circumstances of distress would a default and/or termination right (each as applicable) arise in your jurisdiction?**

The Chilean Civil Code states that the payment of an obligation may be claimed even before the agreed expiration date of the contract, if the debtor is notoriously insolvent or in liquidation. Circumstances triggering default and/or termination rights must be negotiated by the parties on a case-by-case basis. However, please note that the Central Bank has established a two-day banking stay period for the exercise of early termination rights upon the insolvency of a local bank or institutional investor (please refer to question 4.5 below).

**4.2 Are there any automatic stay of creditor action or regulatory intervention regimes in your jurisdiction that may protect the insolvent/bankrupt counterparty or impact the recovery of the close-out amount from an insolvent/bankrupt counterparty? If so, what is the length of such stay of action?**

The Chilean Insolvency Law establishes a 30-day term (which may be extended for up to 90 days) of insolvency protection in favour of the debtor that initiates a reorganisation proceeding to negotiate with its creditors the restructuring of its assets and liabilities. The financial protection period begins when the reorganisation decision is issued by the competent court and

ends with the approval or rejection of the reorganisation agreement proposed by the debtor. Within such protection period, the debtor is prohibited from carrying out certain actions, such as disposing of its assets (other than in the ordinary course of business), and creditors are forbidden from initiating compulsory enforcements of any kind against the debtor or from accelerating their credits. Further, creditors are restricted from early-terminating contracts, as further explained in question 5.3 below.

**4.3 In what circumstances (if any) could an insolvency/bankruptcy official render derivatives transactions void or voidable in your jurisdiction?**

Under The Chilean Insolvency Law, once the reorganisation or liquidation proceedings has begun, the observer (*veedor*) in case of a reorganisation or the trustee (*liquidador*) in case of a liquidation, should file a claw-back action against certain acts or contracts executed by the debtor within one year prior to the beginning of the reorganisation or liquidation proceeding without considering the intent of the parties (i.e., objective claw-back action). Acts and contracts subject to a claw-back during the above one-year period are mainly the following: (a) all prepayments; (b) all payments of past-due debt not made in the manner provided in the original contract; and (c) all mortgages and pledges granted over debtor's assets to secure obligations contracted prior to the respective proceeding. The one-year period is extended to two years in the case of acts or contracts executed without valuable consideration or with related parties of the debtor, including under the guise of an intermediary.

In addition, all acts performed or contracts made by a debtor within two years prior to the beginning of a reorganisation or liquidation proceeding are also subject to a subjective claw-back action, provided the following requirements are met: (a) the counterparty was aware of the poor condition of the debtor's business; and (b) the act or contract causes detriment to the insolvent estate (it being understood that the conditions are detrimental if they diverge from arms-length conditions for comparable transactions) or alters the *pari passu* position that creditors must have in the reorganisation or liquidation proceeding.

**4.4 Are there clawback provisions specified in the legislation of your jurisdiction which could apply to derivatives transactions? If so, in what circumstances could such clawback provisions apply?**

Please see question 4.3 above.

**4.5 In your jurisdiction, could an insolvency/bankruptcy related close-out of derivatives transactions be deemed to take effect prior to an insolvency/bankruptcy taking effect?**

The Chilean Insolvency Law sets forth that upon the occurrence of an acceleration or early termination event related to financial instability, deficient management or other situations existing prior to the mandatory liquidation of a bank or an institutional investor, the acceleration or the termination may only take place after the expiration of the stay period established by the Central Bank in line with recommended international best practices. Pursuant to the law, the Central Bank has established a stay of two banking days as from the date in which the respective event occurred. Acceleration or termination will only be operative upon request of the diligent party made after the expiration of the two-day stay.

**4.6 Would a court in your jurisdiction give effect to contractual provisions in a contract (even if such contract is governed by the laws of another country) which have the effect of distributing payments to parties in the order specified in the contract?**

As previously noted, under Chilean law the formalities of a contract are determined by the law of the country in which the contract is to be executed, but its effects (i.e., the rights and obligations derived therefrom), if the contract is to be performed in Chile, are subject to Chilean law. In this regard, Chilean Civil Code provides for a statutory order of priority for the payments in a bankruptcy scenario. Generally, wages and taxes have preference, as well as credits secured with pledges or mortgages. Unsecured or non-preferential credits (known as *créditos valistas*) have no payment priority unless a subordination agreement among such type of creditors is executed according to Chilean law. In line with the above, a Chilean court would give effect to contractual provisions which have the effect of distributing payments among the parties, to the extent that such provisions do not contravene Chilean statutory order of priority.

## 5 Close-out Netting

**5.1 Has an industry standard legal opinion been produced in your jurisdiction in respect of the enforceability of close-out netting and/or set-off provisions in derivatives documentation? What are the key legal considerations for parties wishing to net their exposures when closing out derivatives transactions in your jurisdiction?**

Yes, Carey has issued advice on enforceability of close-out netting in derivatives transactions addressed to the International Swaps and Derivatives Association, Inc. for its benefit and the benefits of its members.

The general rule under Chilean Insolvency Law is that the liquidation declaration prevents netting of reciprocal obligations which has not taken place by the sole operation of law before the date of the liquidation declaration, except in the case of “connected obligations” (*obligaciones conexas*) derived from the same agreement or negotiation, regardless of their different maturity dates. “Connected obligations” (*obligaciones conexas*) are those obligations that, regardless of whether being in different currencies, emanate from derivative transactions entered into between the same parties, in one or more occasions, under Chilean or foreign law, as part of a single master agreement which has been duly recognised by the Central Bank (e.g., masters agreements indicated in question 1.1 above) and that includes netting provisions in case of voluntary or mandatory liquidation. Each of the obligations arising from derivative transactions executed in accordance with the above, shall be deemed to be due, liquid and immediately enforceable at the date of the liquidation declaration and its amount shall be calculated at such date in accordance with its terms and conditions. In this case, set-off shall be calculated and performed simultaneously on the date of the liquidation declaration.

**5.2 Are there any restrictions in your jurisdiction on netting in respect of all derivatives transactions under a single master agreement, including in the event of an early close-out?**

Please see the answer to question 5.1 above.

**5.3 Is Automatic Early Termination (“AET”) typically applied/disapplied in your jurisdiction and/or in respect of entities established in your jurisdiction?**

As mentioned in question 4.2 above, in the event of a reorganisation plan filed before a Chilean court by a debtor, the debtor is granted with a temporary financial protection period under which the creditor or non-defaulting party is prohibited from early terminating contracts, accelerating debts or enforcing any guarantee or collateral granted to secure its credits based on the filing by the debtor of the reorganisation plan. If the creditor or non-defaulting party breaches this prohibition, the debt arising from the contract that has been early terminated shall be subordinated to the payment of all other debts (preferred and non-preferred) of the insolvent debtor. Therefore, although an AET is typically applied in our jurisdiction, it is advisable to include as an exception to the applicability of the AET, the filing by the Chilean counterparty of a reorganisation request in accordance with Chilean Insolvency Law, from the date of the issuance by the court of the reorganisation decision to the end of the financial protection period. Parties may, however, agree on an AET based on a different event but, the non-defaulting party, would be prohibited from initiating compulsory enforcements or requesting the liquidation of the debtor during the financial protection period.

**5.4 Is it possible for the termination currency to be denominated in a currency other than your domestic currency? Can judgment debts be applied in a currency other than your domestic currency?**

Yes, it is possible for the termination currency to be denominated in a currency other than Chilean pesos.

Although the courts of Chile are empowered to render judgments in a foreign currency and to enforce foreign judgments in such currencies, payments made within an enforcement procedure conducted before Chilean Courts shall be made in Chilean pesos.

## 6 Taxation

**6.1 Are derivatives transactions taxed as income or capital in your jurisdiction? Does your answer depend on the asset class?**

As provided by the Derivatives Taxation Law, derivatives transactions are taxed on the basis of the income arising from derivative transactions. Generally, foreign residents are not subject to taxation in Chile for the income obtained from derivatives transactions, as explained in question 6.2 below.

**6.2 Would part of any payment in respect of derivatives transactions be subject to withholding taxes in your jurisdiction? Does your answer depend on the asset class? If so, what are the typical methods for reducing or limiting exposure to withholding taxes?**

The general rule under the Chilean Income Tax Law is that Chilean-sourced income generated by non-Chilean residents is subject to a withholding tax in Chile. Any gain obtained from assets located in Chile or services rendered in the country are considered to be Chilean-sourced income.

However, according to the Derivatives Taxation Law, income arising from derivatives is deemed to be Chilean-sourced income only when it is accrued or collected by Chilean resident

taxpayers or by a permanent establishment of a foreign entity in Chile. Furthermore, the Derivatives Taxation Law states that income arising from derivatives that are settled by physical delivery of shares or equity rights of companies organised in Chile is also deemed to be Chilean-sourced income.

Whilst the nature of the underlying asset does not determine whether the income obtained from derivatives is subject to taxation in Chile, certain underlying assets are excluded from the application of the Derivatives Taxation Law. Hence, if a non-Chilean resident obtains income from derivatives in which underlying asset precludes the respective transaction from qualifying as a derivative transaction under the Derivatives Taxation Law, it will be subject to withholding tax in accordance with the general rules established in the Chilean Income Tax Law.

### 6.3 Are there any relevant taxation exclusions or exceptions for certain classes of derivatives?

Derivatives Taxation Law establishes an organic tax treatment for derivative instruments and it is applicable to all transactions qualifying as derivatives under such law. The Derivatives Taxation Law considers as “derivative agreements” the following: forwards; futures; swaps and options transactions; and any combination of them, as well as any contract in which its value is calculated in function of one or more variables that determine the corresponding settlement amount and that is recognised and regulated as such according to the legal or regulatory provisions issued by the Financial Market Commission, Pensions Commission and the Central Bank.

The Derivatives Taxation Law also considers as derivative agreements those transactions that are not expressly included in the aforementioned definition, whenever the following requirements are met: (i) their value is calculated as a function of one or more variables which determine the corresponding settlement amount; (ii) they do not require an initial investment or, if they do, the investment is significantly lower than a direct investment in the underlying assets; and (iii) termination is made for a future date, previously determined or determinable.

However, some transactions are expressly excluded as derivatives even if they comply with the abovementioned requirements, such as for example: securities lending made in connection with short sale trades; instruments whose value is linked to the stock value of the issuing entity, such as stock options; weather derivatives; financial asset sale contracts that require asset delivery within the deadlines established by the regulation of the relevant markets; and supply contracts or future rights to services or physical assets such as energy, real estate and supplies, or intangibles such as trademarks and licences.

## 7 Bespoke Jurisdictional Matters

### 7.1 Are there any cross-border issues that apply when posting or receiving collateral with foreign counterparties? For example, are there any restrictions in your jurisdiction on the delivery or acceptance of foreign currencies?

Foreign exchange operations may be freely conducted in Chile. However, the Central Bank may impose limitations and restrictions to the delivery or acceptance of foreign currency. Currently, the only forex limitation contained in the Compendium of Foreign Exchange Regulations of the Central Bank consist of fulfilling certain *ex post* reporting obligations

and conducting transactions in the Formal Exchange Market, which is comprised by banking companies and other entities and persons authorised thereto by the Central Bank.

### 7.2 Are there any restrictions on transferability, for example, assignment and novation (including notice mechanics, timings, etc.)?

Under Chilean law, the assignment of a nominative credit requires the physical delivery by the assignor to the assignee of the title in which the credit is evidenced or recorded. However, such assignment would not be enforceable against the debtor nor third parties, unless it is notified to or accepted by the debtor. In the case of credits that are deemed of a commercial nature and thus subject to the Chilean Commerce Code, the assignment of a nominative credit must be made through a notary public.

The novation by change of creditor requires the explicit release from the first creditor, while the novation by change of debtor requires the explicit release of the former debtor by the creditor, otherwise the new debtor would be deemed only as a deputy for the payment or as a subsidiary or joint and several co-debtor.

### 7.3 Are there any other material considerations which should be taken into account by market participants wishing to enter into derivatives transactions in your jurisdiction?

Given the different types of counterparties and applicable regulatory requirements, it is advisable to engage expert legal advice from the beginning of the negotiations.

## 8 Market Trends

### 8.1 What has been the most significant change(s), if any, to the way in which derivatives are transacted and/or documented in recent years?

A significant change has been the incorporation in 2018 of Chapter III.D.2 to the Financial Regulations Compendium of the Central Bank, which contains provisions applicable to the acknowledgment and regulation of master agreements for bilateral derivatives, where one of the parties is a bank established in Chile or an institutional investor. Further, pursuant to the amendment made to such chapter on December 2019, the Central Bank provided that the occurrence of an event related to financial instability, deficient management or other situations existing prior to the mandatory liquidation of a bank or an institutional investor, permits the early termination and the netting of the corresponding obligations after the expiration of a two-banking day stay counted from the event, as further explained in question 4.5 above.

### 8.2 What, if any, ongoing legal, commercial or technological development do you see as having the greatest impact, positive or negative, on the market for derivatives transactions in your jurisdiction?

The establishment of a new Integrated Information System on Derivatives Transactions and its Operational Regulation is expected to have a major positive impact on the market for derivatives transactions in Chile. The newly created Trade Repository of OTC derivatives transactions provides an infrastructure to register transactions executed by local banks and financial institutions, brokers dealers, funds administrators and other entities

supervised by the Chilean Securities Market Commission, as well as transactions executed by Chilean counterparties with foreign persons, in an efficient, secure and timely manner.

**8.3 In your view, what are the key market trends likely to affect derivatives transactions in your jurisdiction in the upcoming years? For example, the key negotiated commercial terms, the volume of trades and/or the main types of products traded, smart contracts or other technological solutions.**

The Santiago Stock Exchange expects to launch in the second half of 2020 a new Options Market with the following financial

instruments: *Índice de Precios Selectivos de Acciones* (IPSA, the main equities index of the Santiago Stock Exchange); U.S. dollars; and the six most liquid stocks traded in the exchange. This new market will expand the offer of derivatives in the Santiago Stock Exchange, which is currently limited to U.S. dollars, IPSA, UF (*unidad de fomento*, a Chilean currency unit indexed according to inflation) and bonds futures.



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