Financial Statements

Financial Statements of the Central Bank of Chile

Statements of Financial Position as of 31 December 2012 and 2011

(Ch$ million)

Assets	Note	2012	2011
Foreign assets		20,052,478.3	22,020,211.5
Reserve assets	11	19,933,433.5	21,890,542.2
Monetary gold		6,290.6	6,338.5
Special drawing rights (SDR)		579,847.7	633,274.7
Reserve position in the IMF	12	331,087.3	313,531.9
Correspondent banks abroad		9,953.3	406,892.5
Investments in foreign currency:		18,967,149.6	20,511,779.2
Instruments at fair value with effect on net income		16,783,042.3	14,366,374.4
Available-for-sale securities		-	2,115,322.8
Held-to-maturity securities		2,184,107.3	4,030,082.0
Reciprocal loan agreements		38,819.6	18,176.6
Other assets		285.4	548.8
Other foreign assets		119,044.8	129,669.3
Shares of and contributions to the Inter American Development Bank (IDB)		88,111.1	96,001.7
Shares of Bank for International Settlements (BIS)		30,933.7	33,667.6
Domestic assets		3,002,363.2	2,848,169.1
Domestic loans	13	1,110,964.2	956,069.0
Loans to banks and financial institutions		1,110,964.2	956,069.0
Operations under specific legal regulation	14	1,891,399.0	1,892,100.1
General Treasury transfers (Laws 18,267 and 18,401)		260,018.7	253,794.9
Loan for subordinated liabilities of financial institutions (Laws 18,401 and 19,396)		754,321.6	821,311.9
Sinap Liquidation Law 18,900		877,058.7	816,993.3
Other assets		45,002.8	43,526.5
Premises, equipment and intangible assets	15	38,386.8	37,149.1
Other securities		6,146.7	6,106.6
Other current assets		469.3	270.8
Total assets		23,099,844.3	24,911,907.1

Accompanying notes from 1 to 29 are an integral part of these financial statements.

Statements of Financial Position, Continued as of 31 December 2012 and 2011

(Ch$ million)

Liabilities	Note	2012	2011
Foreign liabilities	16	656,457.2	711,843.1
Reciprocal loan agreements		13,253.0	7,097.0
Accounts with international organizations		42,254.1	50,559.6
Special drawings rights (SDR) allocations		600,950.1	654,186.5
Domestic liabilities		26,903,859.3	26,538,327.9
Monetary base	17	7,890,603.7	6,851,171.5
Banknotes and coins in circulation		6,195,118.2	5,265,742.6
Deposits from financial institutions (in Chilean pesos)		965,242.2	676,321.6
Deposits for technical reserve		730,243.3	909,107.3
Deposits and obligations	18	6,108,201.1	6,501,020.3
Deposits and obligations with the General Treasury		694,763.0	861,198.8
Other deposits and obligations		5,413,438.1	5,639,821.5
Documents issued by Central Bank of Chile	19	12,905,054.5	13,186,136.1
Central Bank of Chile bonds in UF (BCU)		8,535,033.3	8,054,639.8
Central Bank of Chile bonds in Chilean pesos (BCP)		3,905,683.5	3,533,333.6
Indexed promissory notes payable in coupons (PRC)		234,221.9	300,176.3
Optional indexed coupons (CERO) in UF		230,094.7	313,339.8
Central Bank of Chile discountable promissory notes (PDBC)		-	984,625.5
Other		21.1	21.1
Other liabilities	20	18,777.3	15,609.2
Provisions		18,365.6	15,247.9
Other securities		411.7	361.3
Net equity	21	(4,479,249.5)	(2,353,873.1)
Capital		(2,355,778.8)	(3,447,503.0)
Valuation accounts		-	1,905.7
(Deficit) surplus for the year		(2,123,470.7)	1,091,724.2
Total liabilities and equity		23,099,844.3	24,911,907.1

Accompanying notes from 1 to 29 are an integral part of these financial statements.

Statements of Income for the years ended as of 31 December 2012 and 2011

(Ch$ million)

	Note	2012	2011
Net income for international reserves	7	203,540.7	449,792.2
Income		707,477.1	650,423.5
Interest income		282,697.8	184,141.6
Gain on sale of instruments at fair value with effect on net income		416,695.8	236,852.2
Gain on sale of available-for-sale securities		6,847.6	6,687.1
Adjustments at fair value		-	219,290.0
Other		1,235.9	3,452.6
Expenses		(503,936.4)	(200,631.3)
Interest expenses		(12.5)	(23.9)
Loss on sale of instruments at fair value with effect on net income		(247,160.9)	(193,299.8)
Loss on sale of available-for-sale securities		(4.3)	(5.0)
Adjustments at fair value		(255,983.3)	(7,302.6)
Other		(775.4)	-
Net income (loss) for other foreign operations		(8,658.6)	1,072.5
Income		662.9	4,590.5
Other income		662.9	4,590.5
Expenses		(9,321.5)	(3,518.0)
Interest expenses		(724.5)	(2,660.3)
Other expenses		(8,597.0)	(857.7)
Net loss for domestic operations	8	(781,373.1)	(707,883.2)
Income		139,008.6	158,150.1
Interest income and adjustments		134,574.9	155,116.9
Other income		4,433.7	3,033.2
Expenses		(920,381.7)	(866,033.3)
Interest expenses and adjustments		(919,868.6)	(865,594.0)
Other expenses		(513.1)	(439.3)
Net gain (loss) on foreign exchange transactions	9	(1,452,858.9)	1,433,546.6
Gain on foreign exchange transactions		661,232.7	1,530,898.3
Loss on foreign exchange transactions		(2,114,091.6)	(97,351.7)
Issuance and distribution costs	10	(37,879.7)	(27,906.4)
Banknotes		(7,884.3)	(14,028.6)
Coins		(29,304.3)	(12,884.5)
Distribution		(691.1)	(993.3)
Personnel and administrative expenses		(43,473.9)	(42,092.1)
Personnel expenses		(26,783.9)	(25,877.2)
Administrative expenses		(12,231.6)	(13,905.0)
Provision for post-employment benefits		(4,458.4)	(2,309.9)
Other expenses		(2,767.2)	(14,805.4)
Depreciation and amortization	15	(2,196.6)	(1,931.2)
Taxes and contributions		(593.6)	(611.7)
Other		23.0	(12,262.5)
(Deficit) surplus for the year		(2,123,470.7)	1,091,724.2

Accompanying notes from 1 to 29 are an integral part of these financial statements.

Notes to the Financial Statements

As of 31 December 2012 and 2011
(Ch$ million)

Note 1 Incorporation and description of business

Central Bank of Chile was established on 21 August 1925, by Decree Law 486. Central Bank of Chile is an autonomous entity of technical nature, full legal capacity, its own assets and indefinite duration, created in accordance with Articles 108 and 109 of the Political Constitution of Chile and ruled by its Basic Constitutional Act.

Central Bank of Chile's objective is to look after the stability of both the Chilean currency and the normal functioning of domestic and foreign payments.

In order to meet its objectives, Central Bank of Chile regulates the amount of money and credit in circulation and executes credit operations and international exchange, such as, dictating regulations on monetary credit, and financial and international exchange matters.

Additionally, Central Bank of Chile is exclusively empowered to issue banknotes and to mint coins.

Central Bank of Chile is domiciled in Santiago de Chile, and its main office is located in Agustinas 1180.

Note 2 Summary of significant accounting policies

(a) Basis of preparation of the financial statements

These financial statements have been prepared in conformity with the "Policies of presentation and preparation of financial reports of Central Bank of Chile" approved by the Central Bank of Chile's Board, pursuant to Resolution 1456-01 dated 15 January 2009 and 1519-01 dated 14 January 2010, having a favorable report by the Superintendence of Banks and Financial Institutions, pursuant to Section 75 of the Central Bank of Chile's Basic Constitutional Act. The policies approved by the Board are consistent with International Financial Reporting Standards (IFRS), issued by the International Accounting Standards Board (IASB), in all areas in which the application of these international accounting standards does not affect legally specified provisions that govern Central Bank of Chile or the compliance with its public duties. Should there be any disagreement; the standards issued by the Board of Central Bank of Chile shall prevail, as in the case of:

a.i The credits related to the liquidation of the *Sinap* governed by Law 18,900, stated in the caption "Operations Under Specific Legal Regulation" are explained in notes 2(k) and 14(b) and valued at amortized cost with effect on net income. The Board of Central Bank of Chile has decided to maintain the accounting treatment this asset had at the original accounting date, as it corresponds to operations arising from specific legal clauses inherent to the Central Bank of Chile' s institutional duties.

a.ii Provisions, assets and contingent liabilities. The Board decided to adopt the criterion of the international standards, however, it will be able to use the power granted by the Central Bank of Chile' s Basic Constitutional Act to record global or individual provisions based upon the risk that may be estimated for certain investing or credit operations. During 2012 and 2011, no provisions were recorded in this regard.

a.iii The statement of changes in equity is not presented. Instead, note 21 Capital and reserves is included; containing the capital movements during 2012 and 2011.

a.iv A statement of cash flows is not presented as defined by the international standard, instead, as part of the notes to the financial statements, a statement of variations in monetary base and a statement of variations in international reserves is presented in note 22.

a.v The statements of comprehensive income are not presented, instead, the statements of income for 2012 and 2011 are presented.

The presentation of these financial statements is framed within an economic and accounting framework that fairly reflects the financial position of Central Bank of Chile, and at the same time, contributes to the economic analysis of Central Bank of Chile' s operations by clearly identifying whether they are undertaken by domestic or foreign agents. From this information it is possible to determine the Central Bank of Chile' s share in the domestic supply of monetary assets and credit and the related effects on the Central Bank of Chile' s foreign creditor position. For this reason, the economic concepts of international reserves and currency issuance are shown under the captions reserve assets and monetary base liabilities, respectively.

The financial statements have been prepared on the historical cost basis. The abovementioned excludes operations corresponding to foreign investments in financial instruments that are reported at their fair value (including the corresponding effect on net income) and available-for-sale securities, which basis of measurement has been performed taking the fair value as reference.

The methods used to measure fair values are presented in note 3.

The English translation of this financial statement is provided as a free translation from the Spanish version (official and binding version). This translation has been performed solely for the convenience of non-Spanish readers.

(b) Functional and presentation currency

As the Central Bank of Chile' s main objective is to look after the stability of the Chilean currency, which implies that open-market operations play a significant role in the development of the monetary policy, accordingly, its main activity is the issuance of banknotes and coins, in Chilean peso, which has been defined as the functional and presentation currency for the financial statements.

The figures of such statements are stated in millions of Chilean pesos, while the figures of these notes are stated in millions of Chilean pesos or U.S. dollars, as applicable, rounded to the nearest decimal.

(c) Transactions in foreign currency and foreign currency translation

The Central Bank of Chile' s functional currency is the Chilean peso. Consequently, all balances and transactions denominated in currencies other than the Chilean peso are considered as denominated in "foreign currency". The balances of the financial statements expressed in this currency are translated into Chilean pesos as follows:

c.i U.S. dollars are translated into Chilean pesos at the closing date "observed U.S. dollar" exchange rate pursuant to Section 44 of the Basic Constitutional Act, that governs Central Bank of Chile, referred to under No. 6 of Chapter I in the "General Provisions" of the Compendium of Foreign Exchange Regulations (*Compendio de Normas de Cambios Internacionales*).

c.ii Assets and liabilities stated in Chilean minted gold, are valued at the average London morning quotation of the "Gold Fixing" rate (U.S. dollars per fine troy ounce), in the morning of the closing business day of the financial statements.

c.iii Translation of foreign currencies other than U.S. dollars is made at the exchange rates published daily by Central Bank of Chile in the *Official Gazette*, which are always based upon the period-end "observed U.S. dollar" rate.

c.iv Special Drawing Rights (SDR) are adjusted at the exchange rates for each of the business days of the month, reported by Central Bank of Chile, except for the last business day of the month in which the exchange rate reported by the International Monetary Fund (IMF) is considered.

The results from the purchase and sale of foreign currency, as well as the differences arisen from the update of the belongings in foreign currency, as a result of the variation of the exchange rates of such foreign currencies compared to the Chilean peso, are recorded as profits or losses for the year.

The main exchange rates to the Chilean peso used as of each year-end are as follows:

	2012 Ch$	2011 Ch$
United States dollar (observed exchange rate)	478.60	521.46
Pound sterling	769.82	802.86
Euro	632.90	675.20
Special Drawing Rights (SDR)	735.57	800.58

(d) General principles used in the preparation of the financial statements

The financial statements have been prepared using as base the recognition of assets, liabilities and results when the flow of future economic benefits is probable from or towards Central Bank of Chile and it is possible to determine a cost reliably, considering for such purpose, the following accounting principles:

d.i Accrual basis
The determination of operating results and the financial position must take into account all the resources and obligations of the period, whether or not they are received or paid, in order for costs and expenses to be properly matched to the revenues they generate. In this regard, the effects of the transactions must be recognized to the extent they generate the right to receive revenues or the obligation to pay for a cost or disbursement rather than when the payment is made or received.

d.ii Going concern
The financial statements are normally prepared on the assumption that an entity is a going concern and will continue in operation for the foreseeable future. Hence, it is assumed that the entity has neither the intention nor the need to liquidate or significantly curtail the scale of its operations.

d.iii Materiality

The relevance of information is affected by its nature and relative importance. Information is material if its omission or misstatement could influence the economic decisions of users taken on the basis of the financial statements. Of course, there is not a boundary line setting the limits of what is significant or not, and the best criterion should be applied to resolve the issues in each case according to the circumstances, taking into account factors such as the relative effects on assets, liabilities, equity, or on earnings for the year.

d.iv Substance over form

If information is to represent faithfully the transactions and other events that it purports to represent, it is necessary that they are accounted for and presented in accordance with their substance and economic reality and not merely their legal form.

d.v Prudence

Prudence is the inclusion of a degree of caution in the exercise of the judgments needed in making the estimates required under conditions of uncertainty, such that assets or income are not overstated and liabilities or expenses are not understated.

(e) Price-level adjustment

The Board decided, upon the favorable report of the Superintendence of Banks and Financial Institutions, to cease the application of comprehensive price-level adjustment as from 2010 in order to adopt the Central Bank of Chile' s financial statements to IFRS, with the condition to protect the application in relation to its equity, from the specific legal regime governing Central Bank of Chile as a public law entity, as well as regarding the payment of paid-in capital and the distribution of the annual surplus to the General Treasury covered by Sections 5, 75, 77, and transitory Article 2 of the Basic Constitutional Act of Central Bank of Chile.

The effect of variations in the exchange rates for assets and liabilities in foreign currencies and indexation on loans and liabilities is included within profit or loss.

In addition, with the purpose of applying the legal regime related to the incorporation of the Central Bank of Chile' s paid-in capital and distribution of surpluses to Tax Authorities as dealt with in Section 5 of the abovementioned legislation, in relation to Sections 75, 77 and transitory Article 2 of the same legislation, Central Bank of Chile decided to record price-level adjustment on paid-in capital for 2012, in memorandum accounts, on the basis of Consumer Price Index variation occurred between 30 November 2011 and 30 November 2012, which was 2.1%.

(f) Interest income and expenses, adjustments and commissions

Interest income and expenses, adjustments and commissions are recognized as net income for the year when earned. Interests are recognized on the basis of their effective rate.

(g) International reserve measurement criteria

International reserves are liquid assets in foreign currency held by Central Bank of Chile. They are instruments supporting monetary and foreign exchange policies, in order to meet Central Bank of Chile' s objective of safeguarding currency stability and the normal functioning of internal and external payment systems. Reserve assets comprise those external assets under the control of the monetary authority, which can dispose of them immediately in order to fund the imbalances of the balance of payments and to indirectly regulate the magnitude of those imbalances.

Investments in foreign financial instruments are recognized at the date of the purchase at its fair value. In addition, these are classified in accordance with IFRS, in the following categories and composition:

g.i Investments at fair value with effect on net income
Includes bonds issued by foreign governments, institutions and banks, mid-term bonds issued by Bank for International Settlements (BIS), treasury bills, discount notes, notes payable in coupons, indexed bonds, secured bonds from public institutions issued by German banks, agency prepayable bonds, agency bills, agency discount notes.

The principle considerations used to classify instruments focus on their high liquidity. They are recorded at fair value and their changes are recognized directly in earnings. The methods used to measure fair values are described in note 3.

g.ii Available-for-sale securities
Includes floating-rate notes, certificates of deposits, floating-rate certificates, commercial papers, bank acceptances, discount term-deposits issued by BIS, negotiable with BIS, term-deposits at interest rates issued by BIS, negotiable with BIS, and BIS floating-rate notes.

They are investments in financial assets that under some market considerations may become effective before their maturity, they are recorded at fair value and the changes in value are recognized directly in equity until the investment is sold or determined to be other-than temporarily impaired, whereupon, the cumulative gains and losses previously recognized in equity are recognized in profit or loss. The methods used to measure fair values are described in note 3.

g.iii Held-to-maturity securities
Includes mostly term and overnight deposits and are investments in financial assets that the entity has the positive intent and ability to hold until maturity; they are valued at amortized cost using the effective interest method. These financial assets are not affected by transaction costs.

g.iv Other financial assets

g.iv.i Reserve position in the International Monetary Fund (IMF): represents the net difference between the assets (installments paid to the IMF for subscription and the net of purchases and repurchases of SDR) and liabilities (deposits made by the IMF) and is classified as a held-to-maturity investment, measured at the cost indexed to Special Drawing Rights (SDR).

g.iv.ii Reciprocal loan agreements: represent the amount owed to Central Bank of Chile by the central banks comprising *Aladi's* Agreement on Reciprocal Payments and Credits for the exports made by Chilean entities. Their classification corresponds to non-derivative held-to-maturity financial instruments, measured at amortized cost.

(h) Shares and contributions to the Inter-American Development Bank (IDB) and contributions to the International Monetary Fund (IMF)

Shares issued by and contributions made to the IDB, and to the IMF, on behalf of the Chilean General Treasury, are stated at acquisition or contribution cost plus adjustments, where applicable.

The accounting treatment of the previously mentioned shares and contributions conformity with Article 3 of DL 2943 dated 1979, published in the *Official Gazette* on 16 November of the same year, according to which such shares and contributions as well as the documents evidencing them, must be recorded for the Central Bank of Chile' s accounting purposes as investments with a charge to its own resources.

Shares and contributions to IDB are shown under "Other foreign assets". Contributions to the IMF are recorded under "Reserve position in the IMF" in "Foreign reserve assets". The "Reserve Position in the IMF" includes the loans granted by Central Bank of Chile to the IMF for involvement in the financing program referred to as "New Arrangements to Borrow" (NAB) and which at year-end was SDR160.5 million. Such loans are a part of the revolving credit facility in favor of the IMF approved by the Central Bank of Chile' s Board on 24 September, 2009 up to SDR1,360.0 million. While as of 31 December 2012 the IMF remaining balance of the revolving credit facility amounted to SDR1,199.5 million, in practice the mechanism operates by calculating quarterly capitalization periods that include the stakeholders' maximum contribution during that period.

(i) Bank for International Settlements (BIS) Shares

During 2003, Central Bank of Chile' s Board Resolutions 1073-04 dated July 10 2003 and 1084-02 dated 16 September 2003, authorized the incorporation of Central Bank of Chile as a member of the Bank for International Settlements (BIS). On 26 September 2003, in accordance with these resolutions, Central Bank of Chile acquired 3,000 shares of the BIS for SDR42,054,000 which are valued at acquisition cost and are shown under "Other Foreign Assets." During 2012, dividends were received in the amount of US$1.4 million (US$1.4 million in 2011).

(j) Domestic loans

Domestic loans are non-derivative financial assets that correspond to loans granted in Chile, classified as held-to-maturity securities, stated with interests and adjustments accrued at year-end and measured at amortized cost pursuant to the effective interest rate method, and are not affected by transaction costs.

Non-adjustable loans are shown at original value or at their latest renewal value and adjustable balances or denominated in foreign currency include the accrued exchange rate and adjustments at the balance date.

(k) Operations under specific legal regulation

Correspond to non-derivative financial assets subject to specific regulatory and legal restrictions such as the loans related to the *Sinap* Liquidation governed by Law 18,900, which are classified as held-to-maturity securities and are measured at amortized cost pursuant to the effective interest rate method, and are not affected by transaction costs.

(l) Premises, equipment and intangible assets

Premises and equipment are measured at acquisition cost, net of accumulated depreciation. The goods that have met their useful life are stated at their residual value considering market reference prices. Depreciation is calculated using the straight-line method.
In 2012, the Bank has recognized costs related to acquisition of licenses and the development of an Integrated Management System (ERP), as well as costs incurred for the SOMA System that is at development stage, as intangible assets. Historical costs are amortized using the straight-line method of accounting over their assigned useful lives.

Depreciation for 2012 and 2011 is recognized as expense and has been calculated considering the following estimated useful lives:

	Years 2012	Years 2011
Buildings	80	80
Furniture and office equipment	10	10
Computer equipment	5	5
Vehicles	5	5
Intangible assets	5	-

(m) Monetary base

Mostly include liabilities of Central Bank of Chile that are part of money, or other financial instruments contribute including freely-circulating banknotes and coins, plus deposits made by the financial system in Central Bank of Chile and the banknotes and coins held on cash by banks. It is recorded at its nominal value.

(n) Deposits and obligations

Deposits and obligations are financial liabilities for deposits and other operations made with the General Treasury and financial institutions, initially measured at fair value, and which are not affected by transaction costs. Subsequently, they are measured at amortized cost pursuant to the effective interest rate method with an effect in earnings. Unadjustable balances are stated at nominal value. Adjustable balances or those denominated in foreign currency include the effect of the accrued exchange rate and adjustments at the reporting date.

(o) Documents issued by Central Bank of Chile

The documents issued by Central Bank of Chile are financial liabilities issued in order to adopt the decisions of monetary policy, initially measured at fair value, and are not affected by transaction costs. Subsequently, they are measured at amortized cost pursuant to the effective interest rate method with effect in earning. Unadjustable balances are stated at nominal value. Adjustable balances or those denominated in foreign currency include the effect of the accrued exchange rate and adjustments at the reporting date.

The following is the detail of held-to-maturity securities: Central Bank of Chile bonds in UF (BCU), Central Bank of Chile bonds in Chilean pesos (BCP), Central Bank of Chile discountable promissory notes (PDBC), Indexed-promissory notes payable in coupons (PRC), Optional indexed coupons (CERO) in UF.

(p) Impairment of financial assets at amortized costs

Regardless of the classification or reclassification of the instruments, in the event it is determined that the recoverable value (fair value) is lower than the earning value recorded in accounting, their impairment shall be recognized with a debit to earning. Pursuant to this policy, during 2012 and 2011, Central Bank of Chile has not recognized any impairment of these financial assets.

(q) Employee benefits

q.i Post-employment benefits

Post-employment benefits are employee benefits which are payable after the completion of employment in Central Bank of Chile, as stipulated in: collective contract between Central Bank of Chile and the Labor Union of Central Bank of Chile, signed on 1 June 2011 and in force up to 30 June 2015; for special resolutions approved by the Board and for special benefits delivered to retired employees of the Former Association of Retired Employees and Beneficiaries of Pensions of Public Officials of Central Bank of Chile. These benefits include: severance indemnities, special indemnity Resolution 1414-01 dated 5 June 2008, special supplementary severance indemnity under the retirement plan per Resolution 1651-06 dated 29 December 2011, special benefits to retired employees of the Former Association of Retired Employees and Beneficiaries of Pensions of Public Officials of Central Bank of Chile.

This recognition is made through an actuarial calculation that considers in both cases demographic and financial variables. It is measured at the current value of all future payments using an annual discount effective interest rate, affected by the expected employment duration and expected lives of beneficiaries.

Actuarial calculation is based on the following assumptions for both years, except for the discount rate which presented a change compared to 2011:

- Mortality rate: Central Bank of Chile used the M-95 mortality table to determine the expected lives of beneficiaries to calculate severance indemnities and RV-2009 to determine the expected lives of beneficiaries for the calculation of post-employment benefits associated with the retirement plan's health plan and benefits of the Former Association of Retired Employees and Beneficiaries of Pensions of Public Officials of Central Bank of Chile.

- Employee turnover: The probabilities of permanence of the employees of Central Bank of Chile were calculated on the basis of the tables prepared by Central Bank of Chile organized in tranches by years of service.

- Salary growth rate: calculated as the annual average composed of the salary growth rate for a five-year period of 5.10% (2011: 5.24%).

- Discount rate: Central Bank of Chile used the annual average of the nominal rate for BCP instruments at 10 years. For 2012, the discount rate was 5.42% (2011: 5.89%).

On 29 December 2011, through Resolution 1651, the Board approved the extension in the Retirement plan applied at Central Bank of Chile since June 2008. This resolution particularly includes individuals joining Central Bank of Chile subsequent to 26 May, 1982 who comply with certain requirements to be eligible for such a plan. These individuals will be entitled to an additional special voluntary indemnity, which will correspond to a third of the monthly gross salary currently received by the employee for each year of service for Central Bank of Chile, over 11 years, as referred to in the preceding paragraph. The amount of the additional indemnity should not exceed an amount equivalent to 11 monthly gross salaries.

q.ii Accrued vacations

The annual cost of employee vacations is recognized in the financial statements on an accrual basis.

(r) Provisions and contingent liabilities

Provisions are liabilities of uncertain timing or amount. These are recognized in the balance sheet when the following requirements are met:

- Is a present obligation arising from past events and,
- At the date of the financial statements it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation; and a reliable estimate of the amount of the obligation can be made.

A contingent liability is an obligation that arises from past events and whose existence will be confirmed only by the occurrence of one or more uncertain future events not wholly within the control of Central Bank of Chile.

(s) Financial derivative instruments

Financial derivative contracts corresponding to forward exchange contracts are initially recognized in the balance sheet at cost and subsequently measured at fair value. Derivative contracts are reported as an asset when their fair value is positive and as a liability when is negative and are included in the captions "Other securities" and "Other deposits and obligations", respectively.

When signing a derivative contract, this is designated by Central Bank of Chile as a derivative security held for trading, as it is not used for hedge accounting purposes.

(t) Use of estimates and judgments

The preparation of financial statements requires management to make judgments, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results may differ from these estimates.

Estimates and underlying assumptions are reviewed on an ongoing basis by Central Bank of Chile' s senior management in order to quantify some assets, liabilities, income, expenses and uncertainties. The revision to accounting estimates is recognized in the period in which the estimate is revised and in any future periods affected.

Information about significant areas of estimation uncertainty and critical judgments in applying accounting policies that have the most significant effect on the amounts recognized in the financial statements are described in the following notes:

- Note 2(l) Premises and equipment, determination of useful life, depreciation and residual value.
- Note 3 Methodology applied for the measurement of international reserve fair values.
- Note 20 Provisions, including severance indemnity and post-employment benefits.

(u) Issued but not yet effective IFRSs

As of the date of these financial statements, there are standards issued by the International Accounting Standards Board (IASB) but they are not effective yet nor is their application mandatory. The following standard and amendments will have an effect on these financial statements when becoming effective:

On 11 May 2011, the IASB issued IFRS 13 Fair Value Measurement. This standard will be effective for the annual periods beginning on 1 January 2013. IFRS 13 establishes in a single standard a framework for measuring fair value of assets and liabilities and includes new concepts and clarification for its measurement. In addition, it requires disclosures by entities on fair value measurements of the fair value of its assets and liabilities. The application of this standard is mandatory for the annual periods beginning on or after 1 January 2013.

Amendment to IAS 19 Employee Benefits: It amends the recognition and disclosure of changes in the defined benefit obligation and plan assets, removing the corridor method and accelerating the recognition of past service costs. The application of this standard is mandatory for annual periods starting on or after 1 January 2013.

IFRS 9 Financial Instruments: Classification and measurement, will replace sections classification and valuation in IAS 39. This standard will be applicable to financial statements of Central Bank of Chile beginning on 1 January 2015 and it shows significant differences when compared to the current standard, including the adoption of a new classification model based on two single categories: amortized cost and fair value; the elimination of current classifications of "Investments held to maturity" and "Available-for sale financial assets", the impairment analysis only of assets stated at amortized cost and the treatment and classification of financial liabilities.

Additionally, there are other standards issued but not yet effective which address matters that do not significantly affect or will not significantly affect the Central Bank of Chile' s operations.

Note 3

Methodology applied for the measurement of fair values

The methodology for the calculation of fair values is applied to financial instruments held as foreign investments, classified as securities at fair value through profit or loss or available-for-sale securities through equity.

The management of international reserves is performed through a world class computer system that includes a methodology for the calculation of fair value. The methodology distinguishes two types of calculation to establish the fair value: priced and non-priced securities.

(a) Priced securities (source: Bloomberg)

The system uses the prices obtained from Bloomberg at the closing of the markets of the current day. The price corresponds to PX Mid = (PX Bid + PX Last)/2.
Where

- PX Mid: Average price
- PX Bid: The last purchase price available for an issuance in a particular day
- PX Last: The last price at which an issuance has been measured in a particular day.

On the other hand, the system calculates the gains and losses from investments on a daily basis using the following formula for 2012 and 2011:

IR Profit/Loss = Total Gain Loss - Accrued Interest – FX Gain/Loss

Where:

- IR Profit/Loss: Interest gain/loss due to price and reference rate changes.
- Total Gain Loss: Total gains and losses.
- Accrued Interest: Portion over the next coupon payment accrued from the last coupon until the calculation date.
- FX Gain/Loss: Gain/Loss due to the effects of foreign currency exchange differences.

(b) Non-priced securities (reference rate)

In regard to the purposes of compliance control, the change in the market value of those securities that do not have any reference prices, it will only have to reflect the straight-line accrual of the reward/discount over the life of the transaction.

The abovementioned, completely removes the effect in the measurement resulting from the changes in the rates (Libid or Libor) and the effect is similar to what it happens with the treatment of deposits.

The fair value of international reserve securities is classified per level as shown in note 11:

- Level 1, quoted market value
- Level 2, measurement with market price
- Level 3, measurement without reference to market price.

Note 4 Segment reporting

In order to meet its objectives, Central Bank of Chile has a number of operating functions and attributions related to the regulation of the money and credits in circulation, the regulation of the financial system and the capital market, the attributions to look after the stability of the financial system, the issuance of banknotes and coins, the functions as fiscal agent, the attributions on international matters and related to operations of international changes and statistic functions.

The Central Bank of Chile' s primary function is the implementation of the monetary policy in Chile. Over 95% of the reserve assets of Central Bank of Chile are managed by Central Bank of Chile' s Financial Operations Division. Additional information on the composition of international reserve assets is presented in note 5.

Note 5 Financial instrument risks

The assets of Central Bank of Chile are mainly composed of financial instruments from international reserves that are traded and kept in custody abroad such as bonds and government notes, bank deposits, among others. The liabilities are comprised of financial instruments related to the management of debt and open-market operations made by the Central Bank of Chile with institutions of the local market through the issuance of notes and time deposits received, among others.

(a) International reserves

International reserves are liquid assets in foreign currency held by Central Bank of Chile to support its monetary and exchange policies. They constitute one of the instruments that Central Bank of Chile has in order to be able to meet the permanent objective of looking after the stability of the currency and normal functioning of domestic and foreign payments.

Consistent with the function of international reserves, as well as with its benefits and costs, the objective of its management aims to provide efficiently a secure access to international liquidity and look after the financial equity of Central Bank of Chile. To achieve this, it acts in conformity with the institutional framework set out in Section 38 of its Basic Constitutional Act, where it is explicitly empowered to manage, maintain and dispose of its international reserves. Central Bank of Chile uses the Wall Street Suite (WSS) system to support its control, investment and operation improvement processes.

a.i Investment policy and referential structure

The investment policy of international reserves considers liquid financial assets meeting the legal requirements established for its administration. It is designed based on its impact on the earnings and risks of Central Bank of Chile financial balance sheet and on the characteristics of the potential foreign currency liquidity needs searching for the preservation of capital in case of possible market fluctuations. However, the new investment policy approved in 2012 particularly included the objective of reducing the cost of maintaining reserves in the margin.

International reserves are grouped in two main portfolios: the investment and liquidity portfolio.

On the basis of the new referential structure, the investment portfolio is made up of three portfolios: (a) Short-term Liquidity; (b) Mid-term Liquidity, and (c) Diversification. This new structure considers lower percentages in U.S. dollars and euros and higher percentages in other currencies; i.e., 47.8% in U.S. dollars, 22.0% in euros, 9.2% in Canadian dollars, 6.1% in Australian dollars, 3.0% in Japanese yen, 2.4% in Swiss francs and 9.5% in other foreign currencies. Additionally, the revised life of the referential portfolio increased from 16.9 to 23.7 months.

Tables 5.1 and 5.2 show a detail of both current and prior benchmarks.

Table 5.1. **Benchmark applicable as of 31 December 2012.**

Portfolio		Share: % over total investment portfolio	Share: % on internal admin	Share: % on sub-portfolio	Length (months)	Benchmark indices
Liquidity	USD	24.0	24.7	100.0	3.7	Merrill Lynch 0 - 1Y
	Total	**24.0**	**24.7**	**100.0**	**3.7**	
Mid-term liquidity	USD	23.8	24.5	39.0	24.5	Barclays 1 - 3Y y 3 - 5Y
	EUR	21.9	22.5	36.0	22.7	
	CAD	9.1	9.4	15.0	22.7	
	AUD	6.1	6.3	10.0	23.2	
	Total	**60.9**	**62.7**	**100.0**	**23.5**	
Diversification	CHF	1.9	2.0	16.0	65.8	Barclays 5 - 7Y y 7 - 10Y Depósito bancario CNH
	CNH	1.9	1.9	15.0	1.5	
	GBP	1.9	1.9	15.0	66.8	
	JPY	2.4	2.5	20.0	70.9	
	KRW	1.9	1.9	15.0	61.1	
	NZD	1.5	1.5	12.0	60.7	
	SGD	0.9	0.9	7.0	69.2	
	Total	**12.4**	**12.6**	**100.0**	**56.3**	
Total internal administration		**97.3**	**100.0**	-	**22.7**	
External administrators	CHF	0.4	16.0	16.0	65.8	Barclays 5 - 7Y y 7 - 10Y Depósito bancario CNH
	CNH	0.4	15.0	15.0	1.5	
	GBP	0.4	15.0	15.0	66.8	
	JPY	0.6	20.0	20.0	70.9	
	KRW	0.4	15.0	15.0	61.1	
	NZD	0.3	12.0	12.0	60.7	
	SGD	0.2	7.0	7.0	69.2	
	Total	**2.7**	**100.0**	**100.0**	**56.3**	
Total investment portfolio		**100.0**	-	-	**23.7**	

Table 5.2. **Benchmark applicable as of 31 December 2011.**

Portfolio		Share: % over total investment portfolio	Share: % on sub-portfolio	Maturity (months)	Benchmark índices
Short-term	USD	30.0	50.0	2.4	Bank risk: Merril Lynch Libid 3 months (USD, EUR, AUD, CAD and GBP) Sovereign risk: Merrill Lynch T. Bills (USD, EUR) and FixBis at 6 months (AUD, CAD and GBP)
	EUR	24.0	40.0	3.9	
	AUD	2.1	3.5	2.8	
	CAD	2.1	3.5	2.8	
	GBP	1.8	3.0	2.8	
	Total	**60.0**	**100.0**	**3.1**	
Long-term	USD	16.7	41.8	38.9	JP Morgan bonds tranches 1 - 3Y, 3 - 5Y, 1 - 10Y
	EUR	13.3	33.3	37.1	
	AUD	1.4	3.5	45.1	
	CAD	1.4	3.5	44.2	
	GBP	1.2	3.0	55.0	
	USD	3.3	8.3	29.5	Barclays Indexed bonds tranche 1 - 10Y
	EUR	2.7	6.8	27.8	
	Total	**40.0**	**100.0**	**37.7**	
Total internal administration		100.0	-	16.9	

The liquidity portfolio is intended to cover the forecasted requirements of funds in the short term. The referential structure of this portfolio is matched in currencies and terms in respect to the forecasted disbursements. The referential structure of the currencies of the liquidity portfolio is defined according to the effective composition of the currencies and the forecasted disbursements and the deposits and withdrawals made by commercial or public sector banks.

a.ii Risk policy and management

The risk management policy defines a number of admissible deviations in respect of the referential structure in terms of maturity, periods, currency and limits over the different types of investment. This policy delimits liquidity, market and credit risks. The operational risk is controlled through the segregation of duties and responsibilities, the application of controls, and internal and external audit exercises over permanent and regular basis. The Departments of International Desk of the Management of International Investments, and Operations Register and Control of the Financial Services Management are responsible for the investments, and their formalization, respectively, while the Manager of Management and Financial Risk Evaluation which reports to the General Manager, measures the performance and risks and verifies the compliance with investment limits.

a.iii Management of liquidity risk

To reduce liquidity risk, a portfolio is mainly structured comprising fixed income securities traded in secondary markets of high liquidity and depth, and to a lesser extent short-term deposits in international commercial banks, with different due dates.

a.iv Management of market risk

Market risk implies possible losses due to variations in the price of investments. The investment policy limits the market risk arising from variations on interest rates and parities by establishing maturity and composition margins of currencies around referential parameters of the portfolios and through the diversification of currencies, securities and investment periods. In the particular case of the diversification portfolio, a risk budget equivalent to 100 basis points is established (ex - ante tracking error). Market risk is monitored through the daily measurement of the maturity and composition of currencies, and by the follow-up of VaR and Tracking Error. The international reserve management monthly report, prepared by the Manager of Management and Financial Risk Evaluation, includes the measurements of performance and risk in an absolute manner and as compared to a benchmark, and presents an evaluation of the implemented investment strategy.

Tables 5.3 and 5.4 set out the different monitored market risk measurements, where the effect of changing the benchmark can be noted, both in terms of length and currency of the portfolios.

Table 5.3. **Market Risk. Internal Investment Portfolio as of 31 December 2012 and 2011.**

		2012	2011
Amount (US$ million)		34,868.4	34,334.4
Length (months)	Portfolio	23.1	18.2
	Departure	0.4	1.0
Breakdown by currency (%)	USD	49.3	48.6
	EUR	22.5	35.8
	JPY	2.4	-
	Other	25.8	15.6
VaR	Absolute (%)	2.2	6.1
	Tracking Error (bp)	4.4	40.8

Annualized VaR and TE calculated using the Variance/Covariance method, with a decline ratio of 0.06 and a standard deviation confidence interval.

Table 5.4. **Market Risk for External Administrator Investment Portfolio as of December 31, 2012 and 2011.**

		2012	2011
Amount (US$ million)		1,024.2	994.6
Length (months)	Portfolio	55.0	40.1
	Departure	(0.9)	3.1
Breakdown by currency (%)	USD	0.4	52.5
	EUR	-	37.4
	JPY	17.9	-
	Other	81.7	10.1
VaR	Absolute (%)	2.4	4.2
	Tracking Error (bp)	29.9	74.6

Source: JPMorgan.

Annualized VaR and TE calculated using the Monte Carlo methodology, with a decline ratio of 0.06 and a standard deviation confidence interval

a.v Management of credit risk

The policies on credit risk refer, on one hand, to the level of diversification allowed among the types of risk, and on the other, to the standards setting the transactions that can be performed by Central Bank of Chile and the method used for performing them. The current policy defines the securities, issuers and counterparties, among other eligible, that may be considered for the investment of international reserves.

Tables 5.5 to 5.8 show the breakdown of reserves by credit rating and type of risk. While the credit rating is an average of the ratings reported by agencies Fitch, Moody's and Standard and Poor's, the types of risks relate to the issuer of the instrument. Banking risk is related to the investment in bank financial instruments; deposits, secured bonds from public institutions issued by German banks. Sovereign risk consists of the investment in securities from sovereign states; deposits, bills, floating rate notes, nominal and indexed bonds. Agency risk is related to the investment in securities from U.S., French and German government agencies; bills, nominal bonds, mortgage-backed securities. Finally, supranational risk is related to the investment in multilateral official issuer securities; deposits, bills, floating rate notes and nominal bonds.

In the Internal Investment Portfolio, and as noted at the end of 2011, sovereign risks concentrate in AAA risk rating, whereas instruments issued by banks concentrate in AA- categories. For external portfolios, sovereign risk decreased its share of AAA risk rating compared to the prior year-end due to the addition of countries with lower risk ratings (China, South Korea and New Zealand) to the benchmark.

Table 5.5. **Breakdown of the Internal Investment Portfolio according to credit risk as of 31 December 2012.**

Credit rating	Type of credit risk (%)				
	Agency	Banking	Sovereign	Supranational	Total
AAA	-	-	92.0	-	92.0
AA	-	-	1.5	-	1.5
AA-	-	1.8	4.3	-	6.1
A+	-	0.4	-	-	0.4
Total	-	2.2	97.8	-	100.0

Table 5.6 **Breakdown of the internal investment portfolio according to credit risk as of 31 December 2011.**

Credit rating	Type of credit risk (%)				
	Agency	Banking	Sovereign	Supranational	Total
AAA	8.9	0.3	75.8	4.8	89.8
AA	-	1.1	0.3	-	1.4
AA-	-	3.0	-	-	3.0
A+	-	2.8	-	-	2.8
A	-	2.7	-	-	2.7
BBB+	-	0.3	-	-	0.3 (*)
Total	8.9	10.2	76.1	4.8	100.0

(*) Corresponds to investments in the Bayerische Landesbank whose last maturity date is 31 January 2012.

Tabla 5.7 **Breakdown of the external administrator investment portfolio according to credit risk as of 31 December 2012.**

Credit rating	Type of credit risk (%)				
	Agency	Banking	Soberano	Sovereign	Total
AAA	-	-	37.0	1.8	**38.8**
AA	-	2.6	12.9	-	**15.5**
AA-	-	7.5	34.1	-	**41.6**
A+	-	1.2	-	-	**1.2**
A	-	2.9	-	-	**2.9**
Total	-	14.2	84.0	1.8	100.0

Tabla 5.8 **Breakdown of the external administrator investment portfolio according to credit risk as of 31 December 2011.**

Credit rating	Type of credit risk (%)				
	Agency	Banking	Soberano	Sovereign	Total
AAA	17.4	-	76.6	3.4	**97.4**
AA-	-	-	0.7	-	**0.7**
A+	-	0.2	0.5	-	**0.7**
A	-	0.5	0.7	-	**1.2**
Total	17.4	0.7	78.5	3.4	100.0

Credit risk may imply possible losses due to the noncompliance with financial operations by the issuers and/or counterparties of Central Bank of Chile.

The investment policy limits the exposures to credit risk of countries, counterparties and issuers, setting amounts and maximum investment maturities that rely on risk ratings reported by rating agencies Moody's, Standard & Poor's and Fitch, and of criteria such as equity and debt, among others. Likewise, the Manager of Management and Financial Risk Evaluation monitors the credit risk on a daily basis by measuring the exposures to different countries, counterparties and issuers and updating regularly risk ratings and other criteria that determine the limits and investment margins.

a.vi Settlement of operations

The Recording and Control of Operations and Payments Departments which report to the Financial Service Management are in charge of this process which corresponds to the stage at which the transactions of financial instruments are executed. They also provide instructions for the transfer of funds from and to other checking accounts that Central Bank of Chile holds abroad.

a.vii Compliance control

The compliance control function is carried out by the Manager of Management and Financial Risk Evaluation and consists of verifying compliance with the limits established in the investment policy. The aspects monitored include: composition of currencies, duration and exposure to credit risk, tracking error limits, among others.

a.viii Custody of securities

Central Bank of Chile operates with the custodians of the following institutions that qualify in accordance with the policies established by the Board: JP Morgan Chase, State Street Bank, and Federal Reserve Bank.

a.ix External administrators

Starting from October 2012, the mandate granted to external administrators, composed of Pacific Investment Management (Pimco) and Goldman Sach Asset Management (GSMA) was amended by standardizing the benchmark to the corresponding internal administration diversification portfolio.

The purpose of such program is to add value to the foreign currency portfolio, obtain knowledge transfer and technology and constitute an active comparison benchmark for the Central Bank of Chile' s portfolio.

(b) Open-market operations

Central Bank of Chile implements its monetary policy through the definition of an objective level for the nominal inter-bank interest rate, known as the Monetary Policy Rate (Tasa de Política Monetaria, TPM in Spanish). In order for the inter-bank rate to be determined at this level, Central Bank of Chile regulates the availability of liquidity (or reserves) of the financial system through several instruments: open-market operations, permanent liquidity and deposit facilities. Cash positions over deposits are also included in the tools of Central Bank of Chile, although Central Bank of Chile does not use them as an active instrument of monetary policy. Open-market operations are mainly performed through periodical biddings of promissory notes issued by Central Bank of Chile, forward purchase and sale contracts for promissory notes and bonds issued by Central Bank of Chile, purchases of debt securities with agreements to resale (Repo), liquidity deposits and foreign currency swaps. In the biddings or auctions the following institutions can participate: financial institutions, pension fund administrators, unemployment fund administrators, insurance companies, mutual funds, brokers and security agents, which operate through the Open-market Operation System (*SOMA* in Spanish), owned and operated by Central Bank of Chile.

The transitory injection of liquidity is performed through overnight Repo transactions with maturities of less than 90 days through permanent liquidity facilities. In the opposite situation, where there is excess of liquidity and the inter-bank rate falls below the objective rate (i.e., the TPM), the transitory excess is withdrawn through liquidity deposits with maturities up to 15 days and a permanent overnight deposit facility. Other instruments used by Central Bank of Chile correspond to the line of credit for liquidity in local currency for secured banks and to the line of credit for liquidity in domestic currency used in special situations.

In order to adequately regulate the daily liquidity of the financial system, Central Bank of Chile prepares a monetary projection detailing the cash position requirement covering the period of measurement.

b.i Risk management policy

Central Bank of Chile' s financial risk management policy controls credit, market and liquidity risks. Operational risk is controlled through the segregation of duties and accountabilities, the application of controls and the performance of external and internal audits on permanent and regular basis. The Domestic Market Management and the Financial Service Management which report to the Financial Operation Divisional are responsible for performing and formalizing operations, respectively and the Department of Manager and Financial Risk Evaluation reporting to the General Management is responsible for issuing and evaluating financial risks managed in the administration of open-market and debt operations.

b.ii Management of credit risk

Credit risk is associated to open-market operations and facilities that inject liquidity to the financial system (Repo, permanent liquidity facility, collateralized credit lines and term liquidity facilities). To mitigate the risk associated to loans to banking institutions under these methods, Central Bank of Chile requires collaterals eligible according to their credit quality, which are valued at market prices at the time of their receipt and subject to the application of discounts or haircuts according to the instrument specific characteristics. The monthly management report on open-market and debt operations prepared by the Manager of Management and Financial Risk Evaluation includes monitoring the exposure to counterparty and collateral risk, as well as measuring debt management and compliance with promissory note and bond bidding programs.

Additionally, Central Bank of Chile conducts the settlement process under the delivery versus payment (DVP) principle with the effective transfer of positions to the account maintained by Central Bank of Chile with *Depósito Central de Valores* (*DCV*), thereby eliminating the main risk. The settlement of the cash component is performed through the payment system referred to as Real Time Gross Settlement System (*Sistema de Liquidación Bruta en Tiempo Real - LBTR* in Spanish), which is owned and managed by Central Bank of Chile, which determines the position of each participant on real time on an individual payment-to-payment basis. This automatically avoids overdrafts and as it simultaneously uses accounts in Central Bank of Chile as settlement asset, it mitigates credit risk.

As of 31 December 2012, loans amounted to MCh$1,065,470.8 for repo transactions and MCh$31,535.2 for permanent liquidity facility agreements. Hundred percent of credit securities received corresponds to bonds and promissory notes issued by Central Bank of Chile.

As of 31 December 2011, loans amounted to MCh$951,674.5 for repo transactions. A percentage of 99.6% of credit securities received corresponds to bonds and promissory notes issued by Central Bank of Chile and the remainder corresponds to mortgage bills issued by financial institutions.

b.iii Management of market risk

Market risk is the risk of potential losses from changes affecting the price or final value of a financial instrument or group of financial instruments. For open-market operations, this risk is mainly associated with changes in the market value of bonds and promissory notes issued by Central Bank of Chile, and the change in value of collaterals received in liquidity injection transactions. For collaterals the risk of value loss is mitigated by using margins and haircuts that write-down their value and allow the effective amount lent to be lower than the collateral received.

For the placement of bonds and promissory notes, risk is mitigated in line with the provisions in current legislation contained in the Compendium of Financial Regulations ruling the placement and adjudication of debt that contemplates the use of competitive bidding processes among financial institutions. Upon issuance of instruments, the main risk is associated with changes in inflation that affect bonds issued in UF.

Monitored market risk indicators include the length and VaR. Tables 5.9 and 5.10 display these indicators and show an increase in the length, the proportional share of instruments denominated in UF in the debt structure and VaR between 2012 and 2011 year-ends. This change is mainly explained by the transitory decision made by Central Bank of Chile of not renewing short-term debt (PDBC) during December 2012

Table 5.9 **Structure and risk of the debt portfolio of Central Bank of Chile as of 31 December 2012.**

Instrument	Ch$ billion	% UF	Holding period (months)
Short-term	-	-	-
Long-term	12,905	70	62.0
Total	12,905	70	62.0

Annualized VaR calculated with a decline ratio of 0.06 and a standard deviation confidence interval.

Table 5.10 **Structure and risk of the debt portfolio of Central Bank of Chile as of 31 December 2011.**

Instrument	Ch$ billion	% UF	Holding period (months)
Short-term	985	-	1,3
Long-term	12,201	71	60.0
Total	13,186	66	57.0

Annualized VaR calculated with a decline ratio of 0.06 and a standard deviation confidence interval.

b.iv Management of liquidity risk

Liquidity risk is the risk of not being able to settle an instrument when necessary or incurring losses when it is necessary to sell it due to a lack of market depth.

For open-market operations, this risk relates to the possibility of issuing bonds and promissory notes or rolling them over in the primary market at prices that are too high compared to securities with similar characteristics traded in the secondary market. This type of risk is mitigated through the provisions in current legislation contained in the Compendium of Financial Regulations that rule the placement and adjudication of debt and by monitoring both secondary and primary markets and their institutions.

Tables 5.11 and 5.12 show a summary of the results of the adjudication of bonds and promissory notes for 2012 and 2011. Note that prices or interest rates for the award of the bidding of bonds and promissory notes are very similar to market rates and demand has been higher than the scheduled securities supply. In comparison to 2011, in 2012 the demand for the securities supplied was higher and spreads in respect to market rates were lower. Another aspect that should be highlighted is that bidding processes for discountable promissory notes issued by Central Bank of Chile PDBCs, were also performed at more convenient rates compared to 2011.

Table 5.11 **Results of the bidding of debt instruments of Central Bank of Chile as of 31 December 2012.**

Instrument	Amount awarded in (Ch$ billion)	Demand (%)	Award (%)	Bidding rate (%)	Market rate (%)	Spread (bp)
PDBC	30,095	152	106	5.00	5.80	(7.6)
BCP	950	342	100	5.35	5.35	0.2
BCU	1,096	285	100	2.43	2.43	(0.2)

Demand and award in respect to the annual bond placement program and monthly discountable promissory notes placement program.
Bidding and market rates correspond to the weighted average for bidding processes during the year.

Table 5.12 **Results of the bidding of debt instruments of Central Bank of Chile as of 31 December 2011.**

Instrument	Amount awarded in (Ch$ billion)	Demand (%)	Award (%)	Bidding rate (%)	Market rate (%)	Spread (bp)
PDBC	29,107	137	102	4.81	4.75	6.4
BCP	1.400	293	104	5.71	5.71	0.1
BCU	3,946	255	106	2.70	2.69	0.7

Demand and award in respect to the annual bond placement program and monthly discountable promissory notes placement program.
Bidding and market rates correspond to the weighted average for bidding processes during the year

Note 6 Changes in accounting policies

As stated in the Central Bank of Chile' s Basic Constitutional Act, title VI, the Board shall, with a prior favorable report from the Superintendence of Banks and Financial Institutions, issue the regulations containing the requirements and general conditions to which the financial statements of the Central Bank of Chile shall conform, to be prepared for periods of one year ending on 31 December of each year.

During 2012, there were no changes in accounting policies compared to 2011.

Note 7 Net income for international reserves

International reserves

For the years ended 31 December 2012 and 2011, this caption is composed of the following:

	(Ch$ million) 2012	2011
(a) Net interests and commissions on:		
Securities at fair value with effect on income	265,084.6	154,058.2
Held-to-maturity securities	16,911.6	28,903.5
Available-for-sale securities	25.1	449.5
Foreign correspondents	664.0	706.5
Subtotal for net interests and commissions	282,685.3	184,117.7
(b) Sales of securities:		
At fair value with effect on income	169,534.9	43,552.4
Available-for-sale	6,843.3	6,682.1
Subtotal for sales of securities	176,378.2	50,234.5
(c) (Loss) gain adjustments at fair value	(255,983.3)	211,987.4
(d) On other income	460.5	3,452.6
Total net income for international reserves	203,540.7	449,792.2

Other foreign operations

Net gain or loss on foreign operations comprise the following:

	(Ch$ million) 2012	2011
On revaluation of accounts with international agencies	(7,006.0)	4,590.5
On interest	(724.5)	(2,660.3)
Other net income and expenses	(928.1)	(857.7)
Total net income for foreign operations	(8,658.6)	1,072.5

Note 8

Net income for domestic operations

For the years ended 31 December 2012 and 2011, this caption is composed of the following:

	(Ch$ million)	
	2012	2011
(a) Income for domestic loan		
Interests	10,754.5	4,859.4
Adjustments	129.4	181.6
Other	4,433.7	3,033.2
Total income for domestic loan	15,317.6	8,074.2
(b) Income for operations under specific legal regulations		
Interests	89,563.9	94,845.9
Adjustments	31,074.9	50,140.4
Total income for operations under specific legal regulations	120,638.8	144,986.3
(c) Income for deposits and obligations held by Central Bank of Chile		
Interests	(96,338.5)	(74,399.3)
Other	(513.1)	(439.3)
Total income for deposits and obligations held by Central Bank of Chile	(96,851.6)	(74,838.6)
(d) Income for documents issued by Central Bank of Chile		
Interests	(613,565.0)	(534,644.2)
Adjustments	(206,912.9)	(251,460.9)
Total income for documents issued by Central Bank of Chile	(820,477.9)	(786,105.1)
Total net income for domestic operations	(781,373.1)	(707,883.2)

Note 9

Net gain (loss) on foreign exchange operations

For the years ended 31 December 2012 and 2011, this caption is composed of the following:

	(Ch$ million) 2012	2011
Gain on foreign exchange operations	661,232.7	1,530,898.3
Loss on foreign exchange operations	(2,114,091.6)	(97,351.7)
Total	(1,452,858.9)	1,433.546.6

Net gain (loss) on foreign exchange operations for each year ended, resulting mainly from the effect of exchange rate differences on foreign currency assets, as follows:

	(Ch$ million) 2012	2011
U.S. dollar	(777,356.0)	843,162.2
Euro	(475,842.3)	397,688.0
SDR	(19,824.5)	21,345.4
Pound sterling	(16,776.9)	40,170.1
Other currency	(159,774.4)	137,068.3
Subtotal net (loss) gain on foreign exchange operations	(1,449,574.1)	1,439,434.0
Arbitrage and other	(3,284.8)	(5,887.4)
Total net (loss) gain on foreign exchange operations	(1,452,858.9)	1,433,546.6

Note 10

Issuance and distribution costs

For the years ended 31 December 2012 and 2011, this caption is composed of the following:

	(Ch$ million) 2012	2011
Banknotes	(7,884.3)	(14,028.6)
Coins	(29,304.3)	(12,884.5)
Distribution	(691.1)	(993,3)
Total	(37,879.7)	(27,906.4)

The increase in currency issuance and distribution costs during 2012 compared to 2011 is due to an increase in the number of coins and banknotes produced and the increase in costs mainly in coins. The detail of banknotes is provided in note 17(a).

Note 11 Reserve assets

This caption includes international reserves held by Central Bank of Chile and is detailed as follows:

	(US$ million) 2012	2011
Monetary gold	13.1	12.1
Special drawing rights (SDR)	1,211.5	1,214.4
Reserve position in the IMF	691.8	601.3
Correspondent banks abroad	20.8	780.3
Investments in foreign currency:	39,630.5	39,335.3
Instruments at fair value with effect on net income	35,067.0	27,550.3
Level 1 market value	35,067.0	27,550.3
Available-for-sale securities	-	4,056.5
Level 3 measurement without reference to market price	-	4,056.5
Held-to-maturity securities	4,563.5	7,728.5
Reciprocal loan agreements	81.1	34.9
Other assets	0.7	1.0
Total reserve assets	41,649.5	41,979.3

As of 31 December 2012, monetary gold amounted to US$13.1 million (US$12.1 million in 2011) equivalent to 7,940 fine gold troy ounces valued at US$1,655.5 per ounce (US$1,531 in 2011). There was no change in the amount of troy ounces compared to 2011.

Special drawing rights (SDR) correspond to reserve assets, equivalent to foreign currencies, assigned by the International Monetary Fund (IMF) to the member countries proportionally to the installment paid and valued in Chilean pesos considering the current parity reported by the International Monetary Fund.

Reciprocal Loan Agreements (debits) represent the amount payable to Central Bank of Chile from the central banks comprising *Aladi's* Agreements on Reciprocal Payments and Credits for the exports performed. Its classification corresponds to non derivative held-to-maturity securities, valued at amortized cost at effective rate.

The decrease observed in reserve assets for the year ended 31 December 2012 of US$329.8 million, compared to 2011, is mainly explained by a decrease in available-for-sale securities of US$4.056.5 million, held-to-maturity securities of US$3,165.0 million and securities at fair value through profit or loss of US$7,516.7 million.

Investments in foreign currencies at each year-end are detailed as follows:

	(US$ million) 2012	2011
U.S. dollar	21,050.7	22,086.6
Euro	7,870.3	12,655.6
Other currencies	12,728.5	7,237.1
Total	41,649.5	41,979.3

Note 12

Reserve position in the International Monetary Fund (IMF)

The reserve position balance in the IMF at each year-end is detailed as follows:

	(Ch$ million) 2012	2011
Subscription installment, contribution	629,721.5	685,378.4
Loan, account No.1	21.2	61.4
New Arrangement to Borrow (NAB)	118,072.3	74,873.6
Deposits	(416,727.7)	(446,781.5)
Total position in the IMF	331,087.3	313,531.9

Note 13

Loans to banks and financial institutions

This caption includes the following operations, which are defined as non-derivative financial instruments held-to-maturity, valued at amortized cost through the effective rate:

	(Ch$ million) 2012	2011
Line of credit on debt restructuring	518.8	1.114.1
Central Bank of Chile repurchase agreements (repo)	1,110.445.4	954,954.9
Total	1,110.964.2	956,069.0

The average purchase rate for Central Bank of Chile repurchase agreements (repo) was 5.07% in 2012 (4.98% in 2011).

Note 14

Operations under specific legal regulations

This caption mainly includes the following operations from specific laws that are defined as non-derivative financial instruments held-to-maturity, valued at amortized cost recognized in profit or loss through the effective rate and which have not been subject to any impairment tests.

a) General Treasury transfers

The item "Tax transfers" under the specific legal regulation in the caption Operations includes the following amounts

	(Ch$ million)	
	2012	2011
General Treasury transfer Law 18,401	260,018.7	253,794.9

In accordance with Article 13 of Law 18,401, differences produced in the recovery, as a result of discounts granted to shareholders of up to UF15 million, will be covered by the General Treasury through future taxes which as of 31 December 2012 amount to Ch$260,018.7 million, equivalent to approximately UF11.4 million (Ch$253,794.9 million in 2011, equivalent to UF11.4 million).

Executive Decree 1526 issued by the Ministry of Finance, dated 14 December 2010, determined the total amount of the transfer that the General Treasury has to perform in favor of Central Bank of Chile because of the application of the abovementioned law for UF11,383,983.4695 and equivalent, at least, to one twentieth of the aforementioned total sum, starting on the eleventh year subsequent to the year in which the aforementioned decree was processed, which corresponds to 25 January 2011. However, this decree expressly contemplates that the General Treasury will be able to make prepayments.

b) *Caja Central de Ahorros y Préstamos* and *Asociación Nacional de Ahorro y Préstamo*

Decree Laws 1381 dated 23 March 1976 and 2824 dated 6 August 1979 regulated the obligation imposed by Central Bank of Chile of granting loans to organizations which were part of the former National Savings and Loan System (*Sinap*), because of the financial position affecting organizations in that system.

Through Law 18,900 dated 16 January 1990, *Caja Central de Ahorros y Préstamos (CCAP)* and *Asociación Nacional de Ahorro y Préstamo* (*Anap*) ceased to exist and a procedure was established through which the respective equity would be liquidated and used to pay shareholders and the obligations of the institutions.

Article 3 of the law established that *Caja Central de Ahorros y Préstamos* shall cease its operations and with consideration of existing commitment, whether it has settled the liquidations required by the law or not, and shall include an inventory of all its rights, obligations and equity and those of the *Asociación de Ahorro y Préstamo*. This account will be submitted to the review of the President of the Republic through the Ministry of Finance. This Article also stipulates the President of the Republic will approve such account through executive decree issued by the Ministry of Finance published in the *Official Gazette*.

Article 5 of the aforementioned law establishes that the General Treasury shall be responsible for any obligations of the *CCAP* and the *Anap* that are not covered upon liquidating shareholders' equity, the funds for which should be requested from the national budget, in conformity with Article 21 of Decree Law 1263 dated 1975.

This loan arises from the grant of refinancing credit lines by Central Bank of Chile to the *Sinap* which had express legal recognition prior to the liquidation of Caja Central de Ahorros y Préstamos and Asociación de Ahorro y Préstamo set out by Law 18,900, in conformity with the aforementioned decree laws, and as included in the operations as of the closing of business on the day before the Central Bank of Chile' s Basic Constitutional Act was enforced, as established in the transitory Article 2 of the law. Consequently, such operations are the opening capital of Central Bank of Chile referred to in Article 5 of such law. The Board has determined to continue applying the accounting treatment this asset had at the date of its initial recognition, as these operations arise from legal specific provisions.

As of 31 December 2012, the amount payable to Central Bank of Chile from the liquidation of these institutions, was Ch$877,058.7 million (this amount includes interest accrued for Ch$542,500.8 million to that date), of which Ch$808,497.7 million correspond to direct loans granted by Central Bank of Chile and Ch$68,561.0 million with credit lines for international organization programs (Ch$816,993.3 million in 2011, of which Ch$751,434.3 million relate to direct loans granted by Central Bank of Chile and Ch$65,559.0 million to credit lines for international organizations programs).

The recovery of such amounts depends on the determination of a specific date for the payment of that loan, from the General Treasury in favor of Central Bank of Chile. For this reason it is not possible to determine the specific date or other conditions on which that payment will be made.

c) Loan for subordinated liability

The balances as of each year-end represent a subordinated liability of *Banco de Chile* with Central Bank of Chile as established in the agreement amending payment terms dated
8 November 1996, in accordance with the provisions of Law 19,396.

On that date, the parent company *Sociedad Matriz del Banco de Chile*, previously referred to as *Banco de Chile*, agreed to transfer the liability to *SAOS S.A.* (*Sociedad Administradora de la Obligación Subordinada*), based on paragraphs three and five of the aforementioned law. Consequently, the liability must be paid in 40 annual, consecutive and equal installments beginning in April 1997.

During 2012, *Sociedad Administradora de la Obligación Subordinada SAOS S.A.* paid UF5,503,988.6769 to Central Bank of Chile, of which UF1,548,166.6602 were allocated to the payment of interests of the debt and UF3,955,822.0167 to the credit amortization for subordinated liability (in 2011 UF5,899,788.7374, of which UF2,280,164.9346 were destined to the payment of interest and UF3,619,623.8028 to amortization).

As of 31 December 2012 the balance amounts to Ch$754,321.6 million (Ch$821,311.9 million in 2011).

Note 15

Premises, equipment and intangible assets

	(Ch$ million) 2012	2011
Premises and equipment, net	36,377.8	37,149.1
Intangible assets, net	2,009.0	-
Total premises, equipment and intangible assets	38,386.8	37,149.1

This caption is mainly composed of the following balances and movements:

	(Ch$ million)				
	Balances as of 31. Dec.11	Acquisitions	Disposals	Depreciation	Balances as of 31.Dec.12
Real estate and facilities	21,553.7	248.9	(212.4)	(231.8)	21,358.4
Furniture and equipment	9,887.5	1,518.2	(149.3)	(1,856.6)	9,399.8
Transport material	390.2	66.8	(49.8)	(80.9)	326.3
Collection of banknotes and coins (*)	3,652.3	-	(24.3)	-	3,628.0
Works of art	1,652.0	-	(0.1)	-	1,651.9
Other	13.4	-	-	-	13.4
Premises and equipment, net	37,149.1	1,833.9	(435.9)	(2,169.3)	36,377.8

(*) This figure includes Ch$24.3 million due to variations in foreign currency exchange of gold pesos.

As of 31 December 2012 and 2011, the caption Depreciation and Amortization of the Statement of Income includes Ch$2,169.3 million and Ch$1,931.2 million, respectively.

Composition and movements of intangible assets:

	(Ch$ million)				
	Balances as of 31. Dec.11	Acquisitions	Disposals	Amortization	Balances as of 31.Dec.12
Computer programs	-	1,636.7	-	(27.3)	1,609.4
Computer programs under development	-	399.6	-	-	399.6
Intangible assets, net	-	2,036.3	-	(27.3)	2,009.0

As of 31 December 2012, the amortization of intangible assets of Ch$27.3 million is recorded under Depreciation and Amortization in the Statement of Income.

Note 16

Foreign liabilities

This caption includes the following operations:

	(Ch$ million) 2012	2011
Reciprocal loan agreements	13.253,0	7.097,0
Accounts with international bodies	42.254,1	50.559,6
Special drawing rights (SDR) allocations	600.950,1	654.186,5
Total foreign liabilities	656.457,2	711.843,1

Reciprocal Loan Agreements (credits) represent the amount owed by Central Bank of Chile to the central banks comprising *Aladi's* Agreement on Reciprocal Payments and Credits for the imports performed. Its classification corresponds to non-derivative held-to-maturity securities, valued at amortized cost at effective rate.

Accounts with international bodies correspond to resources held in local currency by such organizations for its drawing and to obligations of Central Bank of Chile acting as a fiscal agent, with IDB, for promissory notes subscribed in foreign currency in payment of the subscription of shares and capital increases. They do not bear interests, but they do maintain value for the variations of SDR (IMF) and United States dollar by other agencies.

This caption is composed of the following:

	(Ch$ million) 2012	2011
Promissory note obligations with IDB	38,211.9	41,633.9
Inter-American Development Bank (IDB)	3,094.8	7,961.3
Agency for International Development (AID)	901.1	901.1
Multilateral Investment Guarantee Agency (MIGA)	33.0	32.9
International Bank for Reconstruction and Development (IBRD)	13.3	30.4
Total accounts with international organizations	42,254.1	50,559.6

During 2011, Central Bank of Chile recorded in amortization Ch$2,998.4 million of the promissory note liability with IDB, which was financed by the General Treasury in accordance with Section 38 number 2 of the Central Bank of Chile' s Basic Constitutional Act, affecting Central Bank of Chile' s equity in conformity with the provisions of Article 3 of Decree Law 2943 dated 1979.

The assignments of Special Drawing Rights (SDRs) correspond to SDR816,891,579 assigned to Chile through Central Bank of Chile, by the International Monetary Fund, which are subject to possible restitution; they accrue interests on the basis of a rate determined by the IMF on a weekly basis.

Note 17
Monetary base

This caption is composed of the following:

	(Ch$ million)	
	2012	2011
Banknotes and coins in circulation	6,195,118.2	5,265,742.6
Deposits from financial institutions	965,242.2	676,321.6
Deposits for technical reserve	730,243.3	909,107.3
Total monetary base	7,890,603.7	6,851,171.5

(a) Banknotes and coins in circulation

Includes the amount of banknotes and coins of legal tender issued by Central Bank of Chile held by third parties, resulting from the total banknotes and coins received from suppliers and recorded as liabilities at their face value, less the banknotes and coins that are in the cash of Central Bank of Chile and in its vault.

Banknotes and coins in circulation are recorded at face value. The costs of printing and coining are recorded as expense in the caption Issuance and distribution costs.

The distribution of banknotes and coins in circulation as of 31 December of each year is as follows:

	(Ch$ million)	
Denomination	2012	2011
$ 20.000	1,808,594.2	1,421,483.1
$ 10.000	3,390,659.5	2,903,835.5
$ 5.000	418,003.6	399,479.9
$ 2.000	134,675.5	131,463.9
$1.000	161,221.8	151,962.0
$ 500	4,746.8	4,752.0
Other	249.9	251.4
Coins	276,966.9	252,514.8
Total	6,195,118.2	5,265,742.6

(b) Deposits from financial institutions

Deposits from financial institutions reflect the movements in drafts and deposits in local currency resulting from the operations performed by financial institutions with Central Bank of Chile. Their balance represents the funds or resources in favor of financial institutions and is useful for the constitution of cash positions.

(c) Deposits for technical reserve

Deposits for technical reserve refer to compliance with the obligation on technical reserve required from bank institutions under Article 65 of the General Banking Law, which establishes the alternative of maintaining deposits with Central Bank of Chile for those purposes. This law establishes that deposits in current accounts and other demand deposits received by a bank as well as the amounts that it should destine to pay demand obligations which it assumes as a result of performing its line of business, to the extent that they exceed by two and a half times its cash equity, will have to be maintained on hand or in a technical reserve in deposits in Central Bank of Chile or in documents issued by Banco Central of Chile or the General Treasury at any term valued at market price.

Note 18 Deposits and obligations

Deposits and obligations correspond to financial liabilities, classified as held to maturity for deposits held in Central Bank of Chile, by the General Treasury, as well as by financial institutions and are composed of the following:

	(Ch$ million)	
	2012	2011
Deposits and obligations with the General Treasury	694,763.0	861,198.8
Other deposits and obligations	5,413,438.1	5,639,821.5
Total	6,108,201.1	6,501,020.3

(a) "Deposits and obligations with the General Treasury" include:

	(Ch$ million)	
	2012	2011
General Treasury current accounts	626,202.1	795,639.9
Other	68,560.9	65,558.9
Total	694,763.0	861,198.8

(b) "Other Deposits and Obligations" include:

	(Ch$ million) 2012	2011
Permanent Deposit Facility in local currency	3,987,877.9	3,796,300.0
Current accounts in foreign currency	499,231.0	815,359.0
Short-term deposits from bank institutions in foreign currency	890,196.0	993,381.3
Other	36,133.2	34,781.2
Total	5,413,438.1	5,639,821.5

Note 19

Documents issued by Central Bank of Chile

The issuance of documents of Central Bank of Chile is the main supporting element for the implementation of the monetary policy in order to provide liquidity to the market in an efficient manner. These financial liabilities are classified as held-to-maturity and valued at amortized cost through the effective interest method.

As of 31 December 2012 and 2011, maturities of these instruments are as follows:

	(Ch$ million)						
	Up to 90 days	91 to 180 days	181 days to 1 year	Over 1 year to 3 years	Over 3 years	Total 2012	Total 2011
Central Bank of Chile bonds in UF (BCU)	152,767.9	526,141.8	1,168,267.8	226,443.8	6,461,412.0	8,535,033.3	8,054,639.8
Central Bank of Chile bonds in Chilean pesos (BCP)	268,525.7	91,015.4	223,730.4	1,293,525.1	2,028,886.9	3,905,683.5	3,533,333.6
Indexed promissory notes payable in coupons (PRC)	4,493.9	5,509.9	10,447.9	26,096.6	187,673.6	234,221.9	300,176.3
Optional indexed coupons (CERO) in UF	15,797.0	11,468.9	25,433.4	83,119.0	94,276.4	230,094.7	313,339.8
Central Bank of Chile discountable promissory notes (PDBC)	21.1	-	-	-	-	21.1	21.1
Other	-	-	-	-	-	-	984,625.5
Total as of 31 December	441,605.6	634,136.0	1,427,879.5	1,629,184.5	8,772,248.9	12,905,054.5	13,186,136.1

Balances include interest and adjustments accrued as of 31 December 2012 and 2011.

As of 31 December 2012, the net variation of Ch$281,081.6 million in these liabilities compared to 2011, is explained mainly by an increase in the issuance of BCUs, BCPs and a decrease in PDBCs.

In addition, decreases in CEROs in UF and PRCs are due to maturities that have not been renewed during the period and the decrease in PDBCs is attributed to injecting more liquidity into the market.

Note 20 Other liability accounts

This caption is composed of the following:

	(Ch$ million) 2012	2011
Provisions	18,365.6	15,247.9
Other securities	411.7	361.3
Total	18,777.3	15,609.2

Provisions

Central Bank of Chile has recorded provisions for severance indemnity, a benefit established in the Collective Labor Agreement in force for the periods 2007-2011 and 2011-2015 accounted for in accordance with the actuarial method of projected cost. At the same time, the benefits granted to the former Association of Retired Employees and Beneficiaries of Pensions of Public Officials of Central Bank of Chile and healthcare benefits for retirement plans are also included and detailed as follows:

	(Ch$ million) 2012	2011
Balance at the beginning of the year	13,546.1	12,814.1
Provision for the year:		
Severance indemnity	1,147.6	585.8
Special indemnity Resolution 1414-01-080605 and agreed deposit for retirement plan	66.4	90.4
Special indemnity Resolution 1651-06-111229 and agreed deposit for retirement plan	1,752.4	-
Benefits to the former Association of Retired Employees and Beneficiaries of Pensions of Public Officials of Central Bank of Chile	16.6	51.9
Healthcare benefits for retirement plans	(2.7)	3.9
Post-employment benefit provision balance	16,526.4	13,546.1
Pending accrued vacations of personnel	1,836.2	1,698.7
Special indemnity Resolution 572-05-961226	3.0	3.1
Balance at the end of the year	18,365.6	15,247.9

Note 21 Capital and reserves

a) Capital and reserves

Changes in capital and reserves during 2012 and 2011 were as follows:

	(Ch$ million)			
	Capital	Valuation accounts	Net income (loss)	Total
Balances as of 1 January 2011	(1,961,259.2)	1,360.4	(1,489,242.2)	(3,449,141.0)
Deficit distribution as of 2010	(1,489,242.2)	-	1,489,242.2	-
Capital increase (*)	2,998.4	-	-	2,998.4
Valuation accounts	-	545.3	-	545.3
Surplus for the year	-	-	1,091,724.2	1,091,724.2
Balances as of 31 December 2011	(3,447,503.0)	1,905.7	1,091,724.2	(2,353,873.1)
Balances as of 1 January 2012	(3,447,503.0)	1,905.7	1,091,724.2	(2,353,873.1)
Surplus distribution as of 2011	1,091,724.2	-	(1,091,724.2)	-
Valuation accounts	-	(1,905.7)	-	(1,905.7)
(Deficit) for the year	-	-	(2,123,470.7)	(2,123,470.7)
Balances as of 31 December 2012	(2,355,778.8)	-	(2,123,470.7)	(4,479,249.5)

(*) The General Treasury previously provided Central Bank of Chile with Ch$2,998.4 million in 2011 to pay liabilities assumed with IDB, which are registered in Central Bank of Chile' s records as the Fiscal Agent in accordance with the Ordinary Letter issued by the General Treasury 2945 dated 28 October 2011. The recognition of this balance implied recording a capital increase in the same amount (note 16).

Section 5 of the Basic Constitutional Act of Central Bank of Chile established a paid-in capital for Central Bank of Chile at Ch$500,000 million, which at 31 December 2012 corresponds to Ch$2,105,238.3 million adjusted to the Consumer Price Index as of that date, which has to be paid according to transitory Article 2 of the Basic Constitutional Act.

In accordance with Section 77 of the Basic Constitutional Act of Central Bank of Chile, the deficit produced in any year will be absorbed with a debit to constituted reserves.

When there are no reserves or they are insufficient, the deficit produced in any period will be absorbed with a debit to paid-in capital.

As of 31 December 2012, Central Bank of Chile presents negative equity of Ch$4,479,249.5 million (negative equity of Ch$2,353,873.1 million as of 31 December 2011), which is mainly originated from the variations in exchange rate variations of assets in foreign currencies.

Article 11 of Law 20,128 published in the *Official Gazette* dated 30 September 2006 stated that the General Treasury may make capital contributions to Central Bank of Chile through the Ministry of Finance, under the conditions established in such a law for up to five years from the aforementioned date and therefore, such a period finished on 30 September 2011.

b) Price-level adjusted capital

The Board decided no longer to apply comprehensive price-level adjustment to financial statements beginning in 2010, and therefore price-level adjustment on capital is no longer presented in the Balance sheet nor in the Statement of Income, however in order to comply the provisions of Section 5 of the Basic Constitutional Act of Central Bank of Chile, paragraph 2, which states "The capital may be increased by decision of the majority of the Board Members, through capitalization of reserves and adjusted by means of price-level adjustment", as well as stated in Title VI of the same legislation, regarding the distribution of the Central Bank of Chile' s surpluses included in Section 77, and the payment of the initial capital referred to in transitory Article 2. Once the initial capital, properly adjusted as stated in the terms of Section 5 is paid, the resulting surplus for each year, will be determined and calculated for the purposes of surplus distribution to the General Treasury as contained in Section 77, considering the annual adjustment to the equity recorded in memorandum accounts.

As of 31 December 2012, the negative capital price-level adjustment recognized in memorandum accounts amounted to Ch$(53,367.8) million (Ch$(136,459.8) million in 2011), which resulted in adjusted capital of Ch$(2,594,689.9) million (Ch$(3,633,046.3) million in 2011). The amount to price-level adjusted is capital at the reporting date and its respective contributions by the General Treasury, if any, which does not consider valuation accounts. Note that as of to-date the related deficit has not been distributed yet.

		(Ch$ million)	
	Capital as of 31.Dec.12	Price-level adjustment in memorandum accounts	Price-level adjusted total capital as of 31.Dec.12
Balances as of 31 December 2012	(2,541,322.1)	(53,367.8)	(2,594,689.9)

Note 22 Variations in the monetary base and international reserves

According to note 2.(a.vi) and in consideration of Central Bank of Chile' s unique operations, beginning in 2001, instead of preparing a statement of cash flows, Central Bank of Chile discloses a statement of variations in monetary base and a statement of variations in international reserves, defined as follows:

Monetary Base: Central Bank of Chile' s liabilities that form part of money, or otherwise contribute to the formation of monetary aggregates including freely circulating banknotes, coins and checks issued by Central Bank of Chile, plus deposits made by the financial system in Central Bank of Chile.

International Reserves: Foreign assets that are readily available and controlled by monetary authorities for directly financing unbalances, indirectly regulating such unbalances through exchange market intervention and/or for other purposes.

Variations in the monetary base	(Ch$ million) 2012	2011
Initial balance of monetary base	6,851,171.5	5,525,006.6
Increase		
Foreign exchange operations	2,941.6	5,793,799.9
Interest and indexation paid	947,203.3	731,921.9
Domestic loans	134,712.0	951,159.6
Operating support expenses	35,759.3	37,969.0
Securities issued	256,732.4	-
Operations with international bodies	5,416.8	19,163.8
Other assets	1,342.6	-
Total increase	1,384,108.0	7,534,014.2
Decrease		
Deposits and obligations	(220,498. 0)	(1,945,739.8)
Interest and indexation received for domestic operations	(118,078.2)	(131,023.8)
Securities issued	-	(4,120,399.3)
Other minor foreign exchange changes	(6,091.9)	(1,104.1)
Redemption of IDB promissory notes	-	(2,998.4)
Other assets	-	(6,413.1)
Other liabilities	(7.7)	(170.7)
Total decrease	(344,675.6)	(6,207,849.2)
Variation of monetary base for the year	1,039,432.4	1,326,165.0
Final balance of monetary base	7,890,603.7	6,851,171.5

Variations in international reserve assets	(US$ million) 2012	2011
Initial reserve balance	41,979.3	27,863.7
Increase		
Foreign exchange operations	3.0	11,880.9
Deposits and obligations	-	2,230.8
Interests received for deposits and other investment instruments abroad	589.6	2,644.9
Total increase	592.6	16,756.6
Decrease		
Other liabilities	-	(6.0)
Other assets	(0.1)	(0.5)
Deposits and obligations	(890.6)	
Interest paid for other transactions abroad	(83.8)	(2,702.1)
Total decrease	(974.5)	(2,708.6)
Variation in reserves for the year	(381.9)	14,048.0
Effect of exchange rate	52.1	67.6
Final reserve balance	41,649.5	41,979.3

Note 23 Foreign currency balances

The balance sheets include assets and liabilities payable in foreign currencies, whose balances as of 31 December 2012 and 2011 are as follows:

	(US$ million)	
Assets	2012	2011
Foreign assets	41,898.3	42,228.0
Reserves	41,649.5	41,979.3
Other foreign assets	248.8	248.7
Other asset accounts	6.3	430.2
Total assets	41,904.6	42,658.2
Liabilities		
Foreign liabilities	1,363.1	1,348.0
Other foreign liabilities	107.5	93.5
Special drawing rights (SDR) allocations	1,255.6	1,254.5
Domestic liabilities	3,921.3	4,777.8
Deposits and General Treasury liabilities	977.6	1,284.2
Other deposits and obligations	2,943.7	3,493.6
Total liabilities	5,284.4	6,125.8
Net assets	36,620.2	36,532.4

Note 24 Contingencies and commitments

There are lawsuits currently in process against Central Bank of Chile, whose outcomes according to the Central Bank of Chile' s legal department are not expected to have a material effect on equity.

Note 25 Income taxes

Pursuant to Article 7 of Decree Law 3345 dated 1980, Central Bank of Chile is exempt from income taxes.

Note 26 Fiscal agency

Law 20,128 related to General Treasury Liability published in the *Official Gazette* as of 30 September 2006, created the "Economic and Social Stabilization Fund" (*FEES*) and the "Pension Reserve Fund" (*FRP*)". A portion of *FRP* funds is invested in sovereign bonds and other related assets, inflation-indexed sovereign bonds managed by Central Bank of Chile as Fiscal agency and the other portion is invested in corporate bonds and shares managed by an external administrator. In conformity with the provisions of the aforementioned law, the Minister of Finance through Executive Decree 1383, dated 11 December 2006, appointed Central Bank of Chile as Fiscal Agent for the administration of resources referred to such funds, in conformity with the procedures, conditions, methods and other standards established in the aforementioned executive decree.

On 10 January 2011, the Strategic Contingency Fund (*FCE*) has been incorporated in accordance with Executive Decree 19 issued by the Ministry of Finance.

In accordance with Article 5 of the abovementioned Executive Decree 1383, investments of public resources managed by Central Bank of Chile, as Fiscal Agent, have been carried out in accordance with the guidelines established for these effects by the Minister of Finance. These investments have been recorded in off balance sheet accounts.

In accordance with Ordinary Letter 1637 of 18 November 2011 issued by the Ministry of Finance Central Bank of Chile is empowered to outsource part or all of the management of government funds in the *FRP*. Accordingly, in November 2011 BlackRock Institutional Trust Company, N.A. and Rogge Global Partners Plc were selected as portfolio managers for corporate bonds. For share portfolios, BlackRock Institutional Trust Company, N.A. and Mellon Capital Management Corporation were selected as managers and JP Morgan N.A. was selected as custodian, which provides compliance, risk/return assessment, accounting and bookkeeping services.

Through Resolution 1406 of the Board, dated 24 April 2008, *KPMG Auditores y Consultores Ltda.* was assigned as the auditor of the "Economic and Social Stabilization Fund" (*FEES*) and the "Pension Reserve Fund" (*FRP*) for 2012 and 2011. Through an addendum to the audit contract with the audit firm *KPMG Auditores Consultores Ltda.* on 1 October 2011, the audit services on the Strategic Contingency Fund (*FCE*) were incorporated.

Note 27 Transactions with related parties

(a) Central Bank of Chile does not have any related companies.

(b) Compensation of the Board and key executives:

According to Central Bank of Chile' s Basic Constitutional Act, compensation of the Board is set by the President of the Republic for periods not exceeding two years, following a proposal made by a commission formed by former governors and deputy governors of the entity, appointed by the President of the Republic. In order to propose compensation, the act requires them to be based on this compensation paid to the highest-ranked executive positions in bank institutions within the private sector.

Compensation corresponding to the General Manager, the General Counsel and General Auditor of Central Bank of Chile, are at level one of the compensation structure, as they are positions established in Sections 24 through 26 of the Basic Constitutional Act.

The total gross compensation paid to the Board and key executives during 2012 amounted to Ch$1,275.5 million (Ch$1,228.1 million in 2011).

Note 28 Relevant events

Through Executive Decree 167 issued by the Ministry of Finance dated 6 February 2012, and published in the *Official Gazette* on 6 July 2012, the President Mr. Sebastián Pïñera Echenique appointed Mr. Joaquín Vial Ruiz-Tagle as Central Bank of Chile' s Board Member for a period of 10 years starting from the aforementioned date.

Through Resolution 1658E-01 dated 14 February 2012, the Board of Directors of Central Bank of Chile agreed to appoint Mr. Manuel Marfán Lewis as Deputy Governor of the Board until 18 December 2013, when his period of 10 years as a Board Member elapses.

Through Resolution 1660-01 dated 23 February 2012, the Board of Central Bank of Chile agreed to appoint Mr. Gustavo Favre Domínguez as a member of the Audit and Compliance Committee of Central Bank of Chile for a period of three years.

Note 29

Subsequent events

In the opinion of Central Bank of Chile's General Management, between 31 December 2012 and the date of issuance of these financial statements the following subsequent events which could significantly affect the amounts presented in the financial statements have occurred:

(a) Change in US dollar and euro exchange rate

The value of U.S. dollar as of 22 January 2013 was Ch$472.02 representing a decrease of Ch$6.58compared to the rate prevailing as of 31 December 2012. This represents a decrease in Central Bank of Chile' s equity of Ch$113,144.9 million, considering a value of Ch$472.02 per US$1.00.

The value of euro as of 22 January 2013 was Ch$628.61, representing a decrease of Ch$4.29, compared to the rate prevailing as of 31 December 2012. This represents a decrease in Central Bank of Chile' s equity of Ch$25,168.7million, considering a value of Ch$628.61 per €1.00.

The total decrease in Central Bank of Chile's equity due to the drop in the exchange rate for United States dollars and euro on 22 January 2013 is Ch$138,313.6 million.

(b) Approval of financial statements

The financial statements for the year ended 31 December 2012 were presented by the General Manager to the Board on 31 January 2013 and approved for issue at the Meeting 1733.

(c) Other

There are no other subsequent events that might have a significant effect on the figures presented herein or in the Central Bank of Chile' s economic or financial position.

ALEJANDRO ZURBUCHEN SILVA
General Manager

JUAN CARLOS SALAZAR TAPIA
General Accountant

SILVIA QUINTARD FLEHAN
General Auditor

Independent Auditor's Report

The Governor and Board Members of Central Bank of Chile:

Report on the financial statements

We have audited the accompanying financial statements of Central Bank of Chile (the Bank), which comprise the statement of financial position as of 31 December 2012 and 2011, the statement of income for the years then ended and the related notes to the financial statements.

Management's responsibility for the financial statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with the accounting principles described in note 2(a); this includes the design, implementation and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor´s responsibility

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Central Bank of Chile as of 31 December 2012 and 2011 and the results of its operations for the years then ended, in conformity with the accounting principles described in note 2(a) to the financial statements.

Basis of accounting

Note 2(a) to the financial statements describes the basis of accounting on which the financial statements of Central Bank of Chile are prepared in accordance with standards issued by the Central Bank of Chile's Board, as approved by the Chilean Superintendence of Banks and Financial Institutions, as established in Section 75 of the Central Bank of Chile's Basic Constitutional Act. These standards are consistent with International Financial Reporting Standards (IFRS). Should there be any discrepancy, the standards issued by the Central Bank of Chile' s Board shall prevail, including those discussed in note 2(a) to the financial statements in relation to the following matters: a) Accounting treatment of the *Sinap* Liquidation Account Law 18,900 dated 16 January 1990, which is presented within the caption Operations Under Specific Legal Regulation and explained in note 14(b) to the financial statements; and b) Replacement of the Statements of Changes in Equity, Cash Flows and Comprehensive Income with note 21 on Capital and Reserves, Variations in Monetary Base and International Reserve Assets, and Statements of Income, respectively. Our audit opinion is not modified in regard to these matters.

Emphasis on the equity deficit

As discussed in note 21(a) to the financial statements, as of 31 December 2012, Central Bank of Chile has net equity deficit of Ch$4,479,249.5 million ($2,353,873.1 million in 2011), which is explained mainly by changes resulting from the exchange rates of assets denominated in foreign currency.

Other matter

The above translation of the auditors' report is provided as a free translation from the Spanish language original, which is the official and binding version. Such translation has been made solely for the convenience of non-Spanish readers.

Joaquín Lira H. *KPMG Ltda.*

Santiago, 31 January 2013