

corporate governance



Our corporate governance practices are intended to support the Board and senior management in their supervisory work in order to suitably protect the rights of its shareholders and investors.

Corporate Governance Practices

Banco de Chile is a company established in Chile that is listed on the Santiago Stock Exchange, the New York Stock Exchange ⁽¹⁾, the London Stock Exchange and Latibex, a dedicated platform belonging to the Madrid Stock Exchange. Our corporate governance practices are governed by our bylaws, the General Banking Law, the Corporations Law, the Securities Market Law number 18,045 and the regulations of the Chilean Superintendency of Banks and Financial Institutions.

One of the principal objectives of Banco de Chile is to build business relations with its customers, both for their benefit and that of our shareholders, staff and in general the community in which we operate. Our corporate governance practices are intended to support the Board of Directors and senior management in their supervision and management roles, in order to properly protect the rights of our shareholders and investors. By improving our internal self-regulation mechanisms, correctly responding to prevailing regulations and ensuring the consistent commitment to our fundamental principles, we reinforce the creation of long-term value for our shareholders.

Our corporation's priorities are governed by ethical principles in all aspects of our business. The Board of the Bank has

explicitly stated and approved our Ethics Code which sets out the fundamental principles that serve to guide our decisions and lead the organization's business activity. This Code incorporates our fundamental principles like compliance with the law and justice, confidentiality, integrity and responsibility, both corporate and individual.

Our management is guided by the Board of Directors of the Bank, comprising eleven directors and two alternate directors. The complete Board of Directors is elected every three years. The present Board was elected in March 2005 for the period until March 2008. The Chief Executive Officer is appointed by the Board and remains in that position so long as the Board decides. Ordinary Board meetings are held at least once a month. Extraordinary meetings may be called by the Chairman of the Board, by a majority of directors or, in special circumstances, by just one director.

The Board delegates certain functions and activities to the Directors' Committees. This provides for an analysis of specific matters in depth by the committees and provides the Board with the information necessary for the discussion and debate of the general policies and guidelines covering the Bank's business.

In accordance with clause 50 bis of the Corporations Law number 18,046, a Directors' Committee has been formed whose expense budget is approved by the Ordinary

⁽¹⁾ As we are a foreign company, we are not obliged to comply with some of the corporate governance standards set by the New York Stock Exchange (NYSE) but we can be governed by Chilean practices. However, with the exceptions indicated in our web site, our practices comply with the regulations of the NYSE in their most significant aspects.

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we want an accountable Chile

Shareholders Meeting. This Committee is responsible for examining the reports of the external auditors, balance sheets and other financial statements; proposing the external auditors and credit-rating agencies; examining transactions with related companies; and analyzing the remuneration systems and compensation terms of the senior executives.

In view of the growing trend to self-regulation of the financial system and in order to seek greater efficiency from the internal control systems and compliance with local and international regulations, an Audit Committee was formed that concerned itself with the different aspects involved in the maintaining, application and functioning of the Bank's internal controls, the risks implied in the business activities it carries out and compliance with rules and procedures.

Directors' and Audit Committee

The Board meeting (No.2596) of Banco de Chile held on March 24, 2005 agreed that the Directors' Committee would assimilate the functions of the Audit Committee into its own thus creating the Directors' and Audit Committee, assuming the inherent obligations and responsibilities. A new statute was therefore established in accordance with the requirements set out in clause 50 bis of the

Corporations Law number 18,046 and Chapter 1-15 of the Current Rules of the Superintendency of Banks and Financial Institutions.

The same Board meeting agreed to appoint Jorge Awad, who presides it and is the expert member in financial matters, Gonzalo Menéndez and Thomas Fürst as members of the Directors' and Audit Committee. Under Chilean law, the Directors' and Audit Committee should comprise three members, the majority of whom should be independent of the controller. The members of the Committee will remain in their positions for a maximum term of three years or until the end of the term of the Board, if earlier.

As established in the Committee's statutes, the Chief Executive Officer, Legal Counsel and Controller, or their respective deputies, also attend meetings. Meetings may also be attended, as specially invited guests, by a representative at the partner level of the Bank's auditing firm and other persons that the Committee may invite for one or more meetings. The Committee's organization, objectives, responsibilities and scope of its work are contained in the

statutes whose amended and complemented text agreed at the meeting held on July 27, 2005.

The Committee's objectives are to seek the efficiency, maintenance, application and functioning of the internal control systems and compliance with the rules and procedures; supervise compliance of the rules and procedures governing the banking business and identify the business risks of the Bank and its subsidiaries; supervise the functions of the Risk Control Division, ensuring its independence from the management; supervise the functions of the Global Compliance Division, to serve as a link and coordinator of tasks between the internal audit work and the external auditors, also acting as a link between these and the Bank's Board and perform the functions and responsibilities set out in clause 50 bis of the Corporations Law number 18,046.

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The Directors' and Audit Committees were merged into the Directors' and Audit Committee.

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The Committee met on 28 occasions during 2005 and the matters examined included:

- Examination of the fees budgets of the external auditors and credit-rating agencies.
- Analysis of the reports, content, procedures and scope of the inspections of the external auditors and credit-rating agencies.
- Information on and analysis of the annual internal audit program and the results of internal audits and revisions.
- Analysis of the interim and annual financial statements.
- Analysis of the Bank's financial statements included in the form 20-F, for presentation to the Securities and Exchange Commission – SEC (USA).
- Information on the accounting changes occurring during the year and their effects.
- Information on institutional policies concerning due observance of the laws, regulations and internal rules the Bank has to meet.
- Revision of special cases affecting the internal control systems.
- Analysis of the 2005 performance self-evaluation process carried out by the Bank.
- Analysis of related-party transactions, being those referred to in clauses 44 and 89 of the Corporations Law number 18,046.
- Analysis of the remuneration systems and compensation plans for managers and senior executives.
- Information on and analysis of activities relating to foreign branches.
- Analysis of policies relating to operating risk, in the context of Basle II.
- Information on and analysis of matters relating to the Global Compliance Division, principally dealing with the revision of policies for detecting and sanctioning money-laundering transactions and their application.
- Revision of customer communications made through the Superintendency of Banks and Financial Institutions.
- Analysis related to revisions made by the Superintendency of Banks and Financial Institutions.

Loan Portfolio Committee

The principal function of this Committee is to be informed of changes in the composition and risk of the Bank's loan portfolio from both a global perspective and from a sector and line of business point of view. The Committee reviews in detail the principal debtors, the overdue rate, past-due loan indicators, write-offs and allowances for the loan portfolio.

It is also the Committee's function to discuss and prepare proposals for approval by the Board with respect to credit policies, portfolio evaluation methods and the calculation of allowances for doubtful accounts; it is also informed of the allowance sufficiency analysis.

In addition, it authorizes extraordinary write-offs of loans where recovery efforts have been exhausted and controls the liquidation of assets received in lieu of payment.

This Committee comprises five directors plus the Chief Executive Officer, the Credit Risk Division Manager, the Credit Agreement Division Manager and the Risks and Restructuring Control Manager. Meetings are held monthly.

Credit Committee

This Committee is the highest level of approval for credit operation presentations in accordance with the discretionary limit scheme defined by the Board, deciding on business falling within the corporate credit risk criteria (including the Bank, subsidiaries and foreign branches), whose individual and/or group amount for approval is more than UF 250 thousand.

It also approves certain qualitative aspects regardless of the amount submitted for approval, like customers from whom eventual recovery could cause problems affecting the Bank's image, and transactions with related parties.

This Committee is made up of all the directors (minimum quorum of three) and the Chief Executive Officer. The Credit Risk Area and the respective commercial areas submitting the proposals also take part. Meetings are held weekly.

Finance and International Committee

The Finance and International Committee is one for discussion and analysis for the setting of policies with respect to the Bank's financial management. The Committee meets monthly and is composed of five directors, the Chief Executive Officer, the Finance Division Manager, the Corporate and International Division Manager, the Planning and Management Control Division Manager and the Financial Risk Manager. Detailed explanations are made of each of the matters under its responsibility and analyses are made, including the following matters:

- Definition of the policies, procedures and limits with respect to market risk.
- Control and checking of compliance with internal and regulatory limits.
- New financial operations and business.
- Monitoring of positions and related financial risks.
- Control of the use of financial operation counterparty limits.
- Analysis of requirements and composition of liabilities and equity.
- Assignment of the Bank's capital for different asset operations.
- Definitions on the policy for setting the cost of funds.
- Financial management of foreign branches.

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Disclosure Committee

In May 2003, Banco de Chile set up a Disclosure Committee to formalize the steps necessary for ensuring that information given to the market has the necessary accuracy and detail.

This Committee is composed of the Chief Accountant, the Senior Lawyer for international matters, the Risk Control Division Manager, the Global Compliance Division Manager, the Planning and Management Control Division Manager, the Planning and Studies Area Manager and the Investor Relations Manager, who review the quarterly reports and in general all the financial information published by the Bank.

Corporate Risk Management

During December 2005, the Bank set up the Corporate Risk Management that reports to the Directors' and Audit Committee in order to develop the following functions:

- Centralization and coordination of the activities of corporate risk management.
- Implementation of an integrated risk management scheme throughout the organization.
- Provide information to the board for permitting the optimal use of capital.
- Maintain the chief executive officer, and the board, through the Audit Committee, Finance Committee and Portfolio Committee, informed on risk matters.
- Interrelations with regulatory entities.

Global Compliance

During 2005, Banco de Chile began a program for introducing initiatives for reinforcing and ensuring regulatory compliance, especially concerning internationally applicable rules to preventing asset laundering.

In July 2005, the Bank's Board approved the Global Policy on the Prevention of Assets Laundering and Financing of Terrorism, applicable to all its businesses, foreign branches and subsidiaries. This Global Policy was designed to meet the regulatory requirements of all the jurisdictions in which Banco de Chile has a presence, by which it covers the regulatory requirements of the legislation specifically in Chile and the United States of America, as well as the principal international regulations on the subject.

In order to ensure compliance with these regulatory requirements, Banco de Chile Corporation created the Global Compliance Division in April 2005. This Division is independent and reports directly to the Directors' and Audit Committee. It is responsible for all the businesses of Banco de Chile, whether in Chile or the United States of America and includes all the legal vehicles of the Corporation.

The new Division has formed a structure that includes the compliance managers for Chile and the United States of America, responsible for defining specific policies and procedures applicable to the products and services that the Bank and its subsidiaries offer.

In the case of the operation in Chile, the Board approved in September 2005 the modification of the Policy for the Prevention of Asset Laundering and Financing of Terrorism for the businesses of the Bank in Chile; the original version had been approved and implemented in April 2001. The number of analysts was also increased during 2005 for monitoring transactions and their functions were restructured, segmenting them by the different markets of individuals, corporation and private banking. A monitoring unit and regulatory testing unit were also created for ensuring compliance with the policy's requirements. The training plan was also formalized for the new employees and periodic re-training was given to present staff.

The compliance area in Chile has increased the cover of its monitoring by the introduction of new analytical methods, and has begun an evaluation of new software for improving its existing capabilities.

In the case of the branches in the United States of America, the Office of the Comptroller of the Currency (OCC) and the Board of Governors of the Federal Reserve System, through the Federal Reserve Bank of Atlanta, began a revision in September 2004 of our New York and Miami branches. This included an evaluation of, among other things, their compliance with the rules related to the "Bank Secrecy Act" and other regulations for preventing asset laundering. These evaluations detected some deficiencies which resulted in Banco de Chile agreeing with those entities in February 2005 to the issuance of two orders. These led to the preparation of an action plan for ensuring and reinforcing compliance programs under the legislation mentioned above.

Later, on October 12, 2005, Banco de Chile agreed with the OCC and separately with The Financial Crimes Enforcement Network (FinCEN), the imposition of fines on the New York and Miami branches amounting to the sole sum of three million United States dollars with respect to breaches of the "Bank Secrecy Act", in particular, the regulation for the prevention of money laundering and obligations to report suspicious transactions.

Directors' Remuneration and Expenses

The total amount of Directors' remuneration paid during 2005 amounted to Ch\$2,576.1 million, as compensation for their services and attending meetings. No provision has been established for pensions, retirement or other similar benefits for the Directors or other senior executives. The Corporations Law makes no provision for the need to have a Remunerations Committee. By that law, the Directors' Committee should approve the remuneration of senior management.

Further details are provided in Note number 24 to our financial statements 2005.