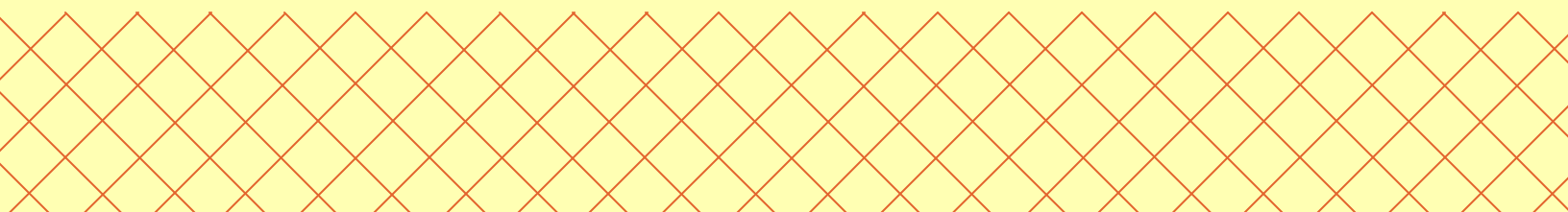


WESTERN HEMISPHERE PAYMENTS AND SECURITIES CLEARANCE
AND SETTLEMENT INITIATIVE
CENTRE FOR LATIN AMERICAN MONETARY STUDIES
THE WORLD BANK

PAYMENTS AND SECURITIES CLEARANCE AND SETTLEMENT SYSTEMS IN COSTA RICA

JUNE 2002



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Foreword

Following a request from the Western Hemisphere Finance Ministers, the World Bank (WB) launched in January 1999 the *Western Hemisphere Payments and Securities Clearance and Settlement Initiative*. The World Bank in partnership with the Centre for Latin American Monetary Studies (CEMLA) leads this initiative. Its objective is to describe and assess the payments systems of the Western Hemisphere with a view to identifying possible improvement measures in their safety, efficiency and integrity. To carry out this mandate an International Advisory Council (IAC) was established in March 1999 comprised of experts in the field from several institutions. In addition to representatives from the WB and CEMLA this Council includes members from the: Bank for International Settlements, Bank of Italy, Bank of Portugal, Bank of Spain, Council of Securities Regulators of the Americas (COSRA), De Nederlandsche Bank, European Central Bank, Federal Reserve Board, Federal Reserve Bank of New York, Inter-American Development Bank, International Monetary Fund, International Organization of Securities Regulators (IOSCO), Securities Commission of Spain, Swiss National Bank and U.S. Securities Commission (SEC).

To assure quality and effectiveness, the Initiative includes two important components. First, all studies are conducted with the active participation of country officials and the project builds on the existing work being undertaken in the respective countries. Second, the Initiative draws on international and national expertise on the subject, through the IAC, to provide guidance, advice and alternatives to current practices.

The Initiative has undertaken a number of activities in order to respond to the Western Hemisphere Finance Ministers' request. These include: the preparation of public reports containing a systematic in-depth description of each country's payments clearance and settlement systems; the delivery of recommendations reports to country authorities on a confidential basis; the organization of IAC meetings to review country studies and provide input for future work; the organization of workshops focusing on issues of particular interest; the creation of a web-page (www.ipho-whpi.org) to present the outputs of the Initiative and other information of interest in the payments systems area; and the promotion of working groups to ensure a continuation of the project activity.

CEMLA has been acting as Technical Secretariat of the Initiative and is playing a major role in making the process sustainable and capable of extension to all the countries in the Hemisphere. To this end, the Initiative has helped strengthen CEMLA's in-house expertise. Additionally, practitioners in payments and securities clearance and settlement in some countries in the Region have participated in the studies under the Initiative, through CEMLA coordination, and this has contributed to the broadening of knowledge and the transfer of know-how within the Region. The endeavors of the working groups in coordination with CEMLA will maintain the infrastructure created under the Initiative and provide a permanent forum for the countries in the Region to discuss, coordinate, and add a collective impetus to the work in the area of payments and securities clearance and settlement systems.

This Report "Payments and Securities Clearance and Settlement Systems in Costa Rica" is one of the public reports in the series and was prepared with the active support of the *Banco Central de Costa Rica* and the *Superintendencia General de Valores* of Costa Rica. The Banco de la República of Colombia, De Nederlandsche Bank and the Swiss National Bank participated directly in its preparation.

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The mission that prepared this Report visited San Jose on June 2001 and consisted of two teams who worked on a coordinated basis in the payments and securities clearance and settlement area. Joaquin Bernal (Banco de la República of Colombia and Working Group on Payment System Issues of Latin America and the Caribbean) was the general coordinator of the mission and of the payments team, which included José Antonio Garcia (CEMLA), also responsible for the preparation of this Report, Massimo Cirasino (World Bank) and Thomas Nellen (National Bank of Switzerland). The securities team included Mario Guadamillas (World Bank) and Jan Woltjer (Bank of Holland), who also helped the payments team. Robert Keppler (World Bank) advised Costa Rica's authorities both in the payments and securities area attending a specific request of these authorities to revise the operational aspects of the systems being developed. The international payments team worked closely with the local team formed by officials of the Central Bank of Costa Rica (Banco Central de Costa Rica, BCCR). Carlos Melegatti (Director of the Financial Services Division) coordinated the local team, which included Francisco Carvajal, Luis Guillermo Zumbado and Renato Montero. The securities team coordinated its work with the local team formed by officials of both the BCCR and the Superintendencia General de Valores (SUGEVAL). Catiana Garcia Kilroy (BCCR Presidency Advisor) coordinated the local team, which included Fiorella Carvajal (SUGEVAL Legal Advisor) and Ronald Santamaria (SUGEVAL Technical Advisor). Ana Laura Sibaja Jimenez, of the Financial Services Division of the BCCR, made important contributions for the preparation of this Report, particularly in the payments sections.

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1 ECONOMIC AND FINANCIAL MARKET OVERVIEW

1.1 OVERVIEW OF RECENT REFORMS

In the past years the Costa Rican institutions involved in the economic reform achieved important changes in the national legislation for the well being of the citizens as well as the economy in general. The planned and materialized solutions that came with the reform respond to different national problems whose causes are both internal and external.

Costa Rica, as well as other nations, modified the development strategy adopted in the previous years. While during the eighties the orientation was on promoting exports, for example through fiscal incentives and capital controls, in the following decade the same orientation was kept but with free mobility of capital. The ultimate strategy has been to attract private capital, particularly with regards to Foreign Direct Investments (FDI).

In the past years Costa Rica signed various free trade agreements, reciprocal investment agreements and other commercial agreements, bilaterally with other countries as well as in a multilateral way with groups of countries or international organizations. Among the latter, Costa Rica signed the Agreement on Subsidies and Compensatory Measures of the World Trade Organization (WTO), according to which, by January 1st 2003, Costa Rica should comply with the agreement, which includes the elimination of the fiscal incentives for exporting companies.

Moreover, economists consider the Costa Rican public debt to be an important problem. According to preliminary statistics of the Central Bank of Costa Rica (*Banco Central de Costa Rica*, BCCR), at the end of year 2001 the internal debt balance was equivalent to 36.5 percent of GDP.

Among other, but particularly for these two reasons, the Costa Rican Parliament issued the Taxing Efficiency and Simplification Law (*Ley de Simplificación y Eficiencia Tributaria*), Law 8114 of July 4th, 2001. This Law modified previous laws related to taxes, among these, the Income Tax Law (Law 7092), the General Sales Tax (Law 6826) and the Consolidation of Consumer Selective Taxes Law (Law 4961). Mainly, tax exemptions were eliminated as well as some minor taxes. The Tax System Rules and Procedures Code was also modified. Among the most relevant changes is the possibility of filing tax returns fully by electronic means under strict security rules such as an access key, smart card and others authorized by the Taxing Authority, which would be equivalent to the taxpayer's signature.¹

In other aspects, regarding social security and pension funds protection, the Costa Rican Parliament issued the Worker Protection Law (*Ley de Protección al Trabajador*), Law 7983, which introduced the complementary pensions regime. In the new regime those funds retained from a worker for retirement are not invested in a common overall fund (distribution regime), but rather a part is sent to an individual capitalization account managed by an authorized pension funds managing firm.

¹ In 2001 a Law Project to regulate the use and the legal recognition of the digital signature was launched. The project, called "*Ley de Firma Digital y Certificados Digitales*", is included in file N. 14.276.

Beside giving the working population the certainty that upon retirement they will have access to a cash flow that has not been affected by inflation, the new regime increases the amount of funds available for investment promoting the development of important institutional investors that demand long term securities, thereby fostering the development of the securities market and the national financial system.

As a complement to this process, the Board of Directors of the BCCR conducted various changes both to the implementation of monetary policy and to the entity's own tasks. For example, last year it agreed on continuing with the reduction of the legal minimum reserve requirement. Since February 1st, 2002 the reserve requirement is 5 percent for all deposits and liabilities, regardless of the currency in which these are denominated.

1.2 MACROECONOMIC BACKGROUND

As a small and open economy, Costa Rica is highly vulnerable to fluctuations in the international economy. This is reflected in the economic figures of recent years. A review of the main economic indicators for the 1996 – 2001 period follows.

1.2.1 Real Sector

The Gross Domestic Product (GDP) increased by 0.9 percent in 2001 compared to 2000. This is the lowest result of the period. Between 1997 and 1999 the highest growth rates, an average of 7.4 percent, were observed. However, starting on year 2000 GDP dynamism began to decrease.

The important growth rates observed from 1997 are linked to the introduction in the country of the firm "*Componentes Intel*"² as well as other high technology companies involved in this sector. Financial reforms and other public policies also helped to improve the climate both for FDI and private domestic investment. Examples of the latter are the expansion of the Export Incentive (*Perfeccionamiento Activo*) and Tax Free Zones (*Zonas Francas*) regimes.³

The slowing down of the high technology industry all over the world by the end of the past decade had an important effect in terms of the value of the national production. This, together with other events such as the reduction in the international prices of several export products and the increase in the price of oil and oil-related products help to explain the lower growth rates of GDP for the 2000-2001 period.

On the other hand, internal demand increased by 4.1 percent in 2001, basically associated with the behavior of investment. While final consumption contributed to GDP growth with 1.2 percent, investment (capital gross formation plus inventory accumulation) had a relative contribution of 3.2

² Intel Corporation started its operations in Costa Rica in 1997. It began exporting electronics in 1998.

³ The production of the Export Incentive Regime and the Tax Free Zones is mainly destined to the external sector and is associated to the transformation of goods and services. Since the end of the 1999 fiscal year several firms decided to move to these regimes, when the government cancelled the Tax Bonus Certificates (*Certificados de Abono Tributario*, CATs) program.

percent. The 15.6 percent growth in investment was associated with a strong accumulation of inventory. Gross capital formation increased only by 3.1 percent.

These events prevented the achievement of the projected 10 percent inflation rate target for 2001. This target was revised at the end of the first semester to 11 percent. This projection was actually the inflation rate observed for year 2001.

The behavior of the unemployment rate during the past six years has been relatively stable, with an average rate of 13.3 percent, slightly below the figure for 2001.

Table 1: Macroeconomics Indicators
(in millions of 1991 colones)

	1996	1997	1998	1999	2000 ^(a)	2001 ^(a)
GDP	1,128,892	1,191,864	1,291,955	1,398,182	1,429,384	1,442,560
GDP (annual growth rate, %)	0.9	5.6	8.4	8.2	2.2	0.9
Consumption (% of GDP)	87.7	87.2	84.5	79.7	79.9	80.4
Gross Capital Formation (% of GDP)	18.8	20.5	23.7	21.0	20.0	20.4
Imports f.o.b. (% of GDP)	36.2	40.9	48.3	44.5	41.7	-41.1
Exports f.o.b. (% of GDP)	32.0	33.0	39.3	44.8	41.4	37.1
BP Current Account (% of GDP)	-2.2	-3.7	-3.7	-4.4	-4.7	-4.1
Global Public Sector (% of GDP)	-4.1	-2.5	-2.0	-3.2	-3.8	-2.9
CPI (annual growth rate, %)	13.9	11.2	12.4	10.1	10.3	11.0
Unemployment Rate (%) ^(b)	13.9	13.1	13.1	13.8	12.0	13.7

Sources: BCCR and Dirección General de Estadísticas y Censos.

^(a) Preliminary figures, except for CPI and Unemployment Rate.

^(b) Measured as Total Underutilization Ratio as of July of every year.

1.2.2 External Sector⁴

The current account of the balance of payments had a deficit of USD 749.9 million⁵ in 2001, USD 7.3 million more than that observed in year 2000. With this result the current account deficit tripled between 1996 and 2001, while in proportion to the GDP it increased from 2.2 percent to 4.1 percent.

Regarding the current account components, the trade balance registered negative balances between 1996 and 2001 except for 1999, when it reached a surplus equal to USD 636.3 million. However, in this same year, the negative result of the “returns” component (particularly the returns on investment⁶) more than offset the surplus of the trade balance.

⁴ Since 1997 the balance of payments of Costa Rica follows the methodology of the 5th Manual for the Balance of Payments of the IMF. The figures for previous years were converted following also the cited methodology.

⁵ Throughout the whole report this symbol ¢ represents the “colon”, the Costa Rican national currency, while USD stands for the dollar of the United States of America.

⁶ The “Returns on Investment” component registers the normal operating profits of firms. In Costa Rica, due to the fact that firms owned by non-residents are more than those owned abroad by residents, normally the balance is negative.

Exports registered an annual average growth of 17.8 percent between 1996 and 1999, while imports had an average growth of 12.5 percent. The observed dynamism of exports stems from the start up of exporting activity by Componentes Intel (1998-1999), the activity peak of the Tax Free Zones and growth of non-traditional exports.

For the years 2000 and 2001 exports experienced a negative growth rate of 12.4 percent and 15.1 percent, respectively. The slowdown of the international market for electronic components and the excessive output of agricultural products (bananas, sugar and coffee) caused by intense competition and the socio-political situation abroad, affected negatively both the exported volume and value and, consequently, the domestic product.

Regarding other components of the current account, tourism revenues are worth mentioning. Tourism revenues increased by USD 514.3 million between 1996 and 2001. Costa Rica is mainly visited by tourists from the United States, South America and the European Union.

As for the financial component of the balance of payments, net FDI stands out. Although not very stable or uniform, the share of this item in the capital and financial account total has never fallen below 64 percent. As mentioned, the Costa Rican development strategy in recent years has aimed at attracting FDI and other private capital in areas of high aggregate value in high technology industries, not only to generate better jobs but also to allow transfers of last generation technology. A major result of this effort was the introduction in the country of Componentes Intel, although other firms such as Procter & Gamble, Baxter, Abbot Laboratories, Western Union and tourist consortia, mainly of U.S., Mexican, Spanish and French origin are also worth mentioning.

Another important element to attract external savings has been the placement of Treasury Bonds, generically known as Eurobonds.⁷ Between 1998 and 2001 USD 1,250 million were issued. Owing to the favorable rating of these issuances, the placement was successful. International reserves grew about USD 400 million in the 1996-2001 period.

Regarding the exchange rate, the policy has been to maintain a stable real exchange rate in order to preserve external competitiveness. The real exchange rate is measured by the ITCER index.⁸ Between 1996 and 2001, the real exchange rate experienced a slight increase (loss of competitiveness) of 5.8 percent.

On the other hand, with the liberalization of the capital and financial account of the balance of payments the determination of the exchange rate has switched from a system of “mini devaluations”

⁷ The first Eurobonds placement was achieved in 1998 and was permitted by Law N. 7671 of May 21, 1997. This Law authorized the placement of up to USD 500 million in the international markets. Then, with Law N. 7970 of December 20, 1999 an additional USD 1,450 million were authorized for the 2000 – 2004 period.

⁸ The Multilateral Effective Real Exchange Rate Index (*Índice de Tipo de Cambio Efectivo Real Multilateral*, ITCER), calculated by the Economic Division of the BCCR, integrates data on inflation and devaluation of a number of countries. Each of these countries is weighted according to its importance on foreign trade for Costa Rica. The ITCER is based on the theory of the Purchasing Power Parity (PPP), whereby external competitiveness is maintained on the basis of balancing the differentials in internal and external inflation through devaluation (appreciation) of the country's currency.

(crawling peg) to one of “directed floating”. The exchange rate is determined in the foreign exchange market (MONED) and the BCCR intervenes to eliminate seasonal or speculative movements in order to maintain the real exchange rate stable. Between December 1996 and December 2001 the nominal exchange rate versus the U.S. dollar increased by ₡121.38, which represents an annual average devaluation of 9.2 percent (see Table 2).

Table 2: Economic Indicators of the External Sector
(in millions of USD)

	1996	1997	1998	1999	2000 ^(a)	2001 ^(a)
I. Current Account	-264.1	-480.9	-520.7	-675.3	-757.2	-749.9
II. Capital and Financial Account	67.5	508.5	547.7	961.7	384.9	463.1
III. Errors and Omissions	111.6	189.1	-176.6	193.6	218.7	298.4
IV. Reserve Assets						
(decrease +, increase -)	84.9	-216.7	149.6	-480.1	153.7	-12.1
V. Balance of Payments	0.0	0.0	0.0	0.0	0.0	0.0
Nominal Exchange Rate (colones per U.S. dollar as of December) ^(b)	219.29	243.55	270.40	297.32	317.40	340.67
ITCER (as of December.)	102.25	99.84	101.49	101.27	98.70	96.65

Source: BCCR.

^(a) Preliminary figures.

^(b) Buy and Sell Average.

1.2.3 Public Sector

The main concern in this sector is the increase of the public debt, whose service absorbs an important percentage of the GDP. The debt has been increasing over the years as a consequence of the need to finance the fiscal deficit.

The global public sector deficit in the year 2001 represented 2.9 percent of the GDP, a high figure that also creates distortions in the financial sector.

In recent years, several high level consulting groups have been created to propose solutions to this problem. One of these proposals has been for the government to sell some of its assets, including State-owned banks. At present the government has been targeting international markets to avoid putting an excessive pressure on the domestic markets. At the same time, this has allowed a better handling of the government cash flow according to the domestic and international interest rate structures.

1.2.4 Monetary Sector

In recent years monetary policy was structured to support the targets in terms of inflation. In this sense, the most dynamic and used instruments were open market operations. In contrast, the

Table 3: Financial Result of the Global Public Sector
(in millions of colones, at the end of each year)

	1996	1997	1998	1999	2000 ^(a)	2001 ^(a)
Global Public Sector	-100,070	-74,802	-72,413	-141,613	-184,903	-157,345
% of GDP	-4.1	-2.5	-2.0	-3.2	-3.8	-2.9
Central Bank of Costa Rica	-38,901	-39,849	-42,203	-71,226	-87,679	-63,579
% of GDP	-1.6	-1.3	-1.2	-1.6	-1.8	-1.2
Non financial Public Sector	-61,169	-34,953	-30,010	-70,387	-97,224	-93,766
% of GDP	-2.5	-1.2	-0.8	-1.6	-2.0	-1.8
Central Government	-99,364	-87,983	-89,232	-99,851	-146,568	-156,708
% of GDP	-4.0	-2.9	-2.5	-2.2	3.0	-2.9
Public Institutions	18,273	26,904	40,798	29,791	38,708	29,801
% of GDP	-0.7	0.9	1.1	0.7	0.8	0.6
Public Enterprises	19,923	26,126	18,424	-327	10,636	33,143
% of GDP	0.8	0.9	0.5	0.0	0.2	0.6

Sources: Autoridad Presupuestaria del Ministerio de Hacienda y BCCR.

^(a) Preliminary Figures.

mandatory reserve requirements for banks became more flexible and saw its importance as a monetary policy instrument diminished. Table 4 presents the main monetary aggregates.

The Monetary Stabilization Bonds (*Bonos de Estabilización Monetaria*, BEMS) balance increased to ₡270,980 million in 2000, about 7.3 times higher than in 1996, and decreased to ₡156,163 million in 2001. During year 2000 (especially the second semester) and 2001, the BCCR needed to gather less resources through the Joint Auction. This was possible because the government paid in advance to the BCCR the documented debt according to Article 175 of the Law 7558 and its reforms.⁹

Regarding the monetary aggregates, the monetary base decreased by 3 percent in 2001 compared to the previous year's balance. This behavior is associated with the drop in the current account deposits with the BCCR, owing to the reduction of the bank reserve requirement (see Table A3 of the Statistical Appendix). As a proportion of GDP, the monetary base decreased less than 1 percent compared to its December 2000 share.

On the other hand, M1 increased in 2001 by 9.7 percent compared to the 2000 balance. The growth of this aggregate goes together with the positive behavior of its components, the currency in the hands of the public (10.5 percent) and the current account deposits in commercial banks (9.3

⁹ This Article provided the documentation of some debts of the central government with the BCCR. In November 1999 the delivery of two long-term securities materialized, one for the amount of ₡183,684 millions and the other for USD 244.3 millions. The debt, which the Monetary Authority had included as a loss, had created a quasi-legal deficit that limited monetary policy management. Practically 100 percent of the debt was paid between the second semester of 2000 and the first quarter of 2001. About ₡790 million (approximately 0.3 percent of the total balance) are still pending.

Table 4: Monetary Aggregates
(in millions of colones and percentages, at the end of each year)

	1996	1997	1998	1999	2000	2001 ^(a)
Monetary Base ^(b)						
Annual Balance	184,122	221,940	242,907	301,650	304,431	295,245
% of GDP	7.5	7.4	6.7	6.7	6.2	5.5
Annual Average of the Monthly Balances	152,335	181,466	203,362	243,237	265,890	252,916
Total Liquidity	805,332	948,184	1,189,841	1,411,024	1,713,375	1,878,349
% of GDP	32.7	31.8	32.7	31.4	35.0	35.4
M1	196,676	281,689	316,310	381,577	443,481	486,585
% of GDP	8.0	9.4	8.7	8.5	9.1	9.2
Quasi-Money	608,656	666,495	873,531	1,029,448	1,269,894	1,391,764
% of GDP	24.7	22.3	24.0	22.9	25.9	26.2
Banking Multiplier ^(c)	1.04	1.10	1.26	1.27	1.38	1.65
Money Circulation Velocity ^(d)	16.2	15.9	14.6	15.2	13.8	12.9
Total Net Internal Credit	650,568	841,563	1,145,403	1,166,002	1,407,666	1,470,440
% of GDP	26.4	28.2	31.5	25.9	28.8	27.7
Public Sector	300,880	397,973	475,589	372,446	370,821	193,180
Private Sector	349,688	443,589	669,814	792,507	1,030,787	1,269,947
Non Banking Financial Sector	N.D.	N.D.	N.D.	1,050	6,058	7,313
BEM Direct Placement	42,714	158,798	158,114	303,884	317,189	161,026
Basic Rate (%)						
In December	24.6	18.5	24.5	18.3	15.5	16.0
Annual Average	24.2	20.9	20.3	22.0	17.1	15.1

Source: BCCR.

^(a) Preliminary figures.

^(b) Includes the commercial banks short-term investment balance in the BCCR.

^(c) Monthly average.

^(d) Ratio between the GDP and M1 (measured as annual average of the daily balances).

percent). This means that the commercial banks increased their capacity to create money, which was reflected in the observed increase of the banking multiplier: for every unit of primary money, payment media expanded 0.3 times more than in 2000.

Beside its relation with a higher dynamism in the national banking system, the latter reflects also the result of the decrease in the legal reserve requirement, which, as previously said, has been gradually reduced in recent years.

Total liquidity increased by 9.6 percent in 2001 compared to the previous year. As a percentage of GDP it had no change. The same stands for its components M1 and quasi-money. In this regard it is worth mentioning that the share of quasi-money in national currency decreased. In 1996 deposits in domestic currency represented almost the 56 percent of the total quasi-money. By 2001 this percentage had decreased nearly 1,600 basis points.

Another indicator, the velocity of money circulation, measured as the ratio between nominal GDP and the average of M1 daily balances, indicates a reduction in the number of times that a monetary aggregate circulates to finance the income flow stemming from the production of goods and services. This trend is explained by a higher growth rate for M1 than for GDP for the last six years. While the monetary aggregate grew by an average of 20.9 percent, nominal GDP increased by 18.6 percent.

Interest rates and the exchange rates are some of the variables in which most of the efforts were concentrated in order to stabilize the economy. During the period being analyzed interest rates were positive and its trend has been consistent with that of international financial markets.

1.3 FINANCIAL SECTOR

As in other countries, especially in Latin America, the Costa Rican financial sector experienced important transformations. For some analysts this is the result of a process that began many years, even decades, ago. The first relevant changes can be traced back to the sixties.

The nationalization¹⁰ of the Costa Rican banking system at the end of the 1940s, together with other measures, produced a high level of repression in the financial sector. The latter discouraged the free and fair access of the different economic agents to financial services, resulting in inefficiencies and other costs for the economy in general. Some of main elements of financial repression were the following:¹¹

- Limitations to some financial and banking entities to perform financial intermediation (not all financial institutions were authorized to receive resources from the public).
- Interest rates, both in colones and in USD, were determined exclusively by the central bank.
- Quantitative and qualitative restrictions to credit.
- Private sector crowding-out because of the public sector hoarding of financial resources.
- Central bank use of direct instruments to execute monetary policy.

The development of private commercial banks began in the mid-eighties. These banks found a market niche that had never received proper attention by the State-owned commercial banks: commercial relations with other countries together with the availability of resources being provided by external agencies for economic cooperation (e.g., *Agency for International Development*, AID).

Thus, the first important changes in the national financial sector took place in the middle of the eighties. Several reforms were implemented, like the Structural Adjustment Programs (*Programas*

¹⁰ Law N. 71 of June 21, 1948.

¹¹ Some of the above mentioned elements have been changed, reducing or totally eliminating the financial repression. In the next chapters several actions taken to speed up the financial sector will be mentioned.

de Ajuste Estructural, PAEs) whose main objective was to allocate scarce economic resources in an efficient way, an issue in which the financial sector has a relevant role.

The first changes had to do with regulation. However, this was not as effective as it had been expected because of the emergence of new financial instruments and entities designed specifically to avoid excessive regulation, the effects of the use of direct instruments by the central bank for monetary control and double taxation (both the profits of financial firms and dividends were being taxed). In these years, a parallel banking system, so called offshore banking, emerged, as well as new instruments such as trusts and other off-balance sheet items, credit and debit cards, leasing, underwriting, factoring, investment funds and pension funds.

The BCCR started to shift its emphasis from direct to indirect monetary instruments, i.e., from the mandatory reserve requirement to open market operations. Additionally the central bank started promoting a deep reform to the financial sector.

1.3.1 Financial System During the Nineties

Having as a basis the changes experienced during the eighties, the financial reform got stronger in the following decade, encompassing banking financial institutions as well as non-banking ones and new financial instruments. The changes included regulatory and supervisory issues as well as modifications in legislation and of monetary and exchange rate policy instruments. Besides enlarging the spectrum of the financial services being offered, the reforms also improved the performance of the financial entities in general in a safer and more open environment. A brief description of some of the changes follows:

- In the area of monetary policy instruments, the most important changes involved open market operations, interest rate controls and the minimum reserve requirement:

Open Market Operations. In 1992 two new open market operations (OMAs) categories were introduced: the money market (*mesas de dinero*) and the auctions. The latter mechanism turned out to be the more important one. In 1996 the BCCR and the Ministry of Finance (*Ministerio de Hacienda*, MH) implemented a joint auction system. Afterwards, in 1997 the joint auction was modified. Starting from this date the auction of Monetary Stabilization Bonds (BEMs) resumed.¹²

With the reforms to the securities market, in the following years other changes were implemented in the auction process. The most important is the issuance of zero-coupon standardized and serialized securities by the MH and the BCCR. At present the securities placement is executed using two mechanisms: "Collection not subject to MH-BCCR auction" and "Joint MH-BCCR auction".

Interest Rates. The BCCR began to progressively relax its controls on interest rates and on the granting of credit. Starting 1992 banks were able to freely determine the rates for loans

¹² Before this modification, only treasury bonds were issued. What the BCCR had actually obtained from the auction was transferred back to the central bank from the government.

granted to the agricultural sector. The rule that compelled banks to maintain 60 percent of their loan portfolio invested in activities considered strategic for development (agriculture, fishing, construction and housing) was also eliminated.

Then, in 1993 financial intermediaries were allowed to freely determine the interest rates for liabilities with a maturity of six months or less. The liberalization of interest rates has been a gradual process and it has encompassed rates for transactions denominated both in domestic as well as in foreign currency.

Minimum Bank Reserve Requirement (Encaje Mínimo Legal, *EML*). As a policy instrument, the EML allows the Monetary Authority to regulate liquidity on the quantity side. On the other hand, for entities subject to reserve this requirement represents a cost that increases financial intermediation spreads. At one time the EML was established at 40 percent for some deposits in national currency. However, since 1996 the Monetary Authority gradually started to reduce and standardize both the required reserve and the liquidity reserve¹³ requirements in an attempt to facilitate the monitoring of such requirements and to reduce the associated financial and economic costs. At present and since February 1st, 2002, the legal reserve requirement and the liquidity reserve are set at 5 percent for all the deposits and liabilities, regardless of their maturities or the currency in which they are denominated.

- After the economic crisis that began in the first part of the eighties, the BCCR monopolized the operations in foreign currency. For this reason the exchange rate liberalization and the opening of the capital account of the balance of payments in 1992 was beneficial both for State-owned and for private commercial banks as well as other non-banking financial institutions, as it allowed them to develop new channels for financial intermediation.¹⁴

In the years following the financial reform of 1995 the most important event was the approval of the Regulations for Foreign Exchange Transactions.¹⁵ These regulations had been modified several times since then, for example, on issues such as how the BCCR determines the reference exchange rate or how the position in foreign currency of each institution participating in the foreign exchange market is determined.

¹³ The financial entities not subject to a minimum reserve requirement must hold a liquidity reserve on the total amount of funds collected from the public and the contributions of workers and associates. Although similar to the EML, it differs in the following aspect: while 100 percent of the funds corresponding to the reserve requirement must be deposited in the BCCR, the liquidity reserve must be invested in securities or deposit instruments of the National Banking System, including the BCCR and the Central Government. According to the Guidelines of Monetary Policy Regulations of February 16, 1996, these instruments must be highly liquid, safe and profitable.

¹⁴ Foreign currency contracts were legalized. This helped not only the financial entities but also other economic agents. The rules exporters had to comply with regarding the disclosure and settlement of foreign currencies were relaxed.

¹⁵ The Regulations for Foreign Exchange Transactions had been ruling since their publication in the "Gazette" in October 10, 1997. These regulations target transactions made with foreign currencies throughout the national territory, according to the Organic Law of the Central Bank of Costa Rica (Law 7558 of November 27, 1995).

- The most important change in the financial legislation was the new Organic Law of the Central Bank of Costa Rica (LOBCCR), Law 7558 of November 27, 1995. This law breaks the monopoly of the State-owned banks over the deposits of the public and allows private banks to increase the number of services and financial instruments offered to the public.¹⁶

Law 7558 worked as a catalyst for the integral reform of the financial sector, particularly in terms of the organization, regulation and supervision of the financial entities, pension funds and the securities market. Some changes were simultaneous while others occurred in the following years.

Once the supervision of financial entities was declared as of national interest in the new LOBCCR, the “Financial Entities General Audit” (*Auditoría General de Entidades Financieras*, AGF) was replaced by the General Superintendency of Financial Entities (*Superintendencia General de Entidades Financieras*, SUGEF). This produced a substantial change in the supervisory function, moving its focus from an “auditing” perspective to “prudential supervision” whose objective is to anticipate possible crises using early warning indicators and to foster an orderly exit of troubled institutions. In 1997 a Regulation for the constitution, transfer, registry and functioning of financial groups was approved.¹⁷ The minimum equity requirement for private banks and non-banking financial firms was increased to \$1,250 million and \$250 million, respectively. This increase was applied gradually and concluded in 1999.¹⁸

- In the pensions sector, the first change was produced with the enactment of the Law for the Private Regime for Complimentary Pensions, Law 7523 of August 18, 1995, whose objective is to authorize and regulate private plans and systems for complimentary pensions and individual savings, whose purpose is to provide additional protection against risk associated with aging and death.¹⁹ The Superintendency of Pensions (*Superintendencia de Pensiones*, SUPEN) was also created with this Law. This Superintendency falls under the umbrella of the BCCR and started activities in August 1996.

Once SUPEN was established, a discussion over the creation of an integrated system of pensions started and it materialized with the enactment of the Law for the Protection of Workers (*Ley de Protección al Trabajador*), Law No. 7983 of February 11, 2000.

- The reform was extended to the securities market in 1997. After thorough analysis and discussion a new Securities Market Law (*Ley Reguladora del Mercado de Valores*, LMV), Law 7732, was enacted in the first quarter of 1998. The former National Securities

¹⁶ The reform to the Article 59 of the Organic Law of the National Banking System N. 1644 broke the monopoly of the state bank over the checking and savings deposits collection. However, private banks must comply with some requirements to access to this right, according to the same Article.

¹⁷ This regulation indirectly supervises the offshore entities.

¹⁸ The social capital revision of the Banks and of the financial entities is done with the objective of avoiding excessive risks for the institutions (moral hazard).

¹⁹ Article 1, Chapter I of the Law N. 7523.

Commission (*Comisión Nacional de Valores*) was replaced by the Superintendency of Securities (*Superintendencia General de Valores*, SUGEVAL). The former modifications also included changes to the structure, powers and organization of the new Superintendency.

The National Council for Financial System Supervision (*Consejo Nacional de Supervisión del Sistema Financiero*, CONASSIF) was also created with this Law. Its role is to determine the rules by which the financial system superintendencies must abide. Thus, CONASSIF rules the activities of SUGEF, SUGEVAL and SUPEN.

- With the enactment of the new LOBCCR in 1995 a great number of pending tasks emerged for the Monetary Authority. Some of these have already been accomplished with the transformation of financial supervision and regulation, of the superintendencies, CONASSIF and the BCCR itself. According to Articles 68 and 69 of the LOBCCR, another pending task was the development of the payments system. This was accomplished with the development of the Interbank Trading and Electronic Payments System (*Sistema Interbancario de Negociación y Pagos Electrónicos*, SINPE).

The first steps in this direction coincided with the development of the clearinghouse for cheques and electronic funds transfer. Currently the SINPE comprises the following services: clearing and settlement house (CLC, for cheques and other securities), the Electronic Funds Transfers between banks as well as between third parties (TI and TT, respectively), Tax Information and Settlement (ILI), Direct Debits (DD), Direct Credits (CD) and the External Services Settlement Facility (LSE). Because of its importance for the economy, the SINPE project is currently a key working area of the BCCR Division of Financial Services (see Chapter 4).

This overview of the reforms and transformations of the Costa Rican financial sector was not intended to cover all the aspects involved in the reform effort. As a matter of fact, in recent years, some modifications to the mentioned laws and others have been made. Also, an important number of rules have been implemented in order to regulate financial activity and protect participating economic agents. However, not in all cases the actual outcome was the one expected and some modifications to adapt the financial and technological transformations of the sector remain pending. The Legislative Assembly is currently discussing a Law Project²⁰ which will modify once again the LOBCCR, the Organic Law of the National Banking System (*Ley Orgánica del Sistema Bancario Nacional*, LOSBN), the Securities Market Law (*Ley Reguladora del Mercado de Valores*, LMV) and other laws that have an effect on the activities of the BCCR. With this new reform the intention is to eliminate some distortions and differences still existing in the sector by, for example, giving more autonomy to the BCCR, fostering a higher level of competitiveness and establishing a mechanism to provide protection for small depositors.

1.3.2 National Banking System

The LOSBN states that private banks must constitute themselves as companies, or, if not possible, as unions or cooperatives. According to the Commercial Code, these legal figures must be located in

²⁰ File N. 14.286.

the national territory. For this reason in Costa Rica there are no branches of foreign banks, which does not inhibit the possibility for foreign investors to participate in these companies.

According to the Fifth Report on Foreign Direct Investment (FDI) in Costa Rica,²¹ while in 1997 the FDI in the financial sector was negative by USD 0.2 million, the estimates for 2001 indicate that it was approximately USD 29.8 million (equivalent to 7 percent of total FDI expected for 2001). The FDI for 1999, which includes the acquisition of the *Banco Banex* by the *Corporación del Istmo of Panama*, was significant at USD 93.4 million. Prior to the acquisition the *Corporación del Istmo* had maintained in Costa Rica the *Banco del Istmo*; however, this commercial name disappeared with the acquisition and the name *Banco Banex* prevailed. The estimates for 2001 indicate that 11 financial entities, of which 10 are banks and only one is a non-banking institution, will receive FDI. These capital flows come basically from Panama, Nicaragua and the United States.

Although the merger by acquisition mentioned above is the most important of the past years in Costa Rica, it is not the only one. The increase in minimum capital requirements, the policy of attracting private capital and the consolidation trend of financial groups between 1996 and 2001 resulted in various mergers and acquisitions. As a consequence of these actions and the liquidation of some entities, while in 1996 the 25 private banks had been authorized and were controlled by SUGEF, this number decreased to 16 for year 2001. Even so, it is possible to say that the sector actually grew and consolidated.²²

Regarding commercial banks, comparing the deposit balances according to the currency in which they are denominated, it is observed that between 1996 and 2001 deposits in local currency increased slightly more than those in foreign currencies (both in nominal terms and measured in the respective currency). However, putting together the balances of both currencies (using as a conversion factor the annual bid and ask accrued average) it is observed that the share of deposits in foreign currency became higher. This could be evidence of a small change in the preferences of the public. Nonetheless, domestic currency denominated deposits continue to be the most significant part, with 53 percent of the total balance in 2001 (see Table 5).

In recent years the commercial banks, especially those that are privately owned, increased the number of agencies and automated teller machines (ATMs), particularly in the San Jose metro area but also in more distant locations.²³ Also, a large number of banking entities and non-banking financial entities modified their traditional working hours (Monday to Friday 9.00 a.m. to 4.00 p.m.) increasing the number of daily hours and opening on Saturdays as well.

²¹ Document elaborated by the FDI Inter-Institutional Group comprised by BCCR officials (Balance of Payments) Costa Rican Tourism Institute (ICT), CINDE, External Commerce Ministry (COMEX), and Procomer. The document was published in June 2002. For more details, the complete report can be found at the BCCR's website (www.bccr.fi.cr).

²² Some research papers of the Division of Economic Studies of the BCCR dealing with concentration indexes for the banking industry (Herfindal and C4) may be consulted for more details. The papers are available at www.bccr.fi.cr.

²³ For more details, see Statistical Appendix, Series A tables.

Table 5: Deposits in Commercial Banks
(in millions of colones (national currency items) and USD million (foreign currency items))

	1996	1997	1998	1999	2000	2001 ^(a)
Exchange Rate (colones/USD) ^(b)	207.7	232.6	257.2	285.7	308.2	328.9
<i>In National Currency</i>						
Checking Account Deposits	104,933	174,874	192,144	237,313	300,454	328,495
Savings Deposits	43,817	58,476	72,001	79,037	135,725	157,440
Term Deposits and Investment Certificates	270,122	248,252	287,395	335,341	367,918	343,722
<i>In Foreign Currency</i>						
Checking Account Deposits	116	122	152	244	296	416
Savings Deposits	181	211	246	246	372	460
Term Deposits and Investment Certificates	865	978	1,237	1,304	1,392	1,386

Source: BCCR.

^(a) Preliminary figures.

^(b) Annual accrued average of buy and sell.

Particularly during year 2001 some banks began to transform their Internet sites into electronic banking access sites (e-banking). Such sites, together with the telephone, are currently the most popular methods to execute banking operations from remotely. Among the e-banking services the clients may use are the payment of utilities, payment of loans and new loan applications, balance enquiry, credit card payments (issued by the same institution), term investments and balance transfers between accounts (intrabank).

In general, commercial banks are the most important sector within the national financial system. Mutu²⁴ (*mutuales*) follow banks in importance in terms of assets, loans, and deposits, while for indicators like equity, other financial entities occupy the second place.

1.4 CAPITAL MARKETS

The Costa Rican securities market consists almost totally of transactions that are executed using the trading facilities of the stock exchange. Currently, one stock exchange is operating in Costa Rica, the *Bolsa Nacional de Valores* (BNV).²⁵ Both debt issues and stocks are traded at the BNV. Since the Securities Market Law (SML) states that buy and sell transactions of publicly offered securities (including repos) are to be performed exclusively by the respective members of the stock exchange²⁶

²⁴ "Mutual" is the legal term used to make reference to those financial entities authorized by the National Housing Financial System (*Sistema Financiero Nacional de Vivienda*) exclusively to perform this kind of financial intermediation.

²⁵ Up to January 1999 two stock exchanges were operating in Costa Rica, the *Bolsa Nacional de Valores* and the *Bolsa Electrónica*. Then, through a merger the *Bolsa Nacional de Valores* remained as the sole stock exchange in the country.

²⁶ Article 23 of the SML.

(brokerage firms, called "*Puestos de Bolsa*"), the over-the-counter market (OTC) in Costa Rica is limited to individual bonds issuances made by entities controlled by the SUGEF.²⁷

The Costa Rican securities market is clearly dominated by the public sector (basically the MH and the BCCR). These securities represented about 92 percent of the total value traded in 2000. In this same year repo operations²⁸ represented about 62 percent of the secondary market transactions. Repos are normally short term (1 to 7 days) and the underlying securities are basically those issued by the public sector. The stability of the share of repo operations in total transactions in recent years seems to indicate that an important part of the stock exchange activity consists of money market or liquidity transactions.

Stocks represent merely 0.3 percent of total value traded. On the other hand, the important growth in secondary market transactions relative to the total amount of transactions at the BNV, from 33 percent in 1997 to 73.5 percent in 2000, is evidence of its growing depth.

Stock exchange transactions are executed through different electronic trading platforms operated by the BNV. Through the TEDEL system the following operations are executed: spot and forward transactions and repos, with a settlement cycle of T + 1. The Liquidity Market (*Mercado de Liquidez*) is a trading system for overnight repos with MH or BCCR securities that settles in T. There is also a new platform called "SITE", designed for standardized securities, with a settlement cycle of T + 3 for stocks and T + 1 for international bonds, mainly Eurobonds issued in Costa Rica in USD. Finally, there is a "Primary Auction" (*Subasta Primaria*) platform in which public securities are traded every 14 days and private securities, mainly short-term securities such as certificates of deposit issued by financial institutions, are traded daily. In this last system settlement takes place in T + 2.

On the other hand, there is the Interbank Money Market (*Mercado Interbancario de Dinero*, MIB) operated by the Instituto Centroamericano de Finanzas y Mercado de Capitales (ICAF), which in turn is owned by the BNV. Only banks and the BCCR may participate in the MIB (i.e., the intermediation of a *Puesto de Bolsa* is not required).²⁹ Although a private company operates the MIB, its rules are actually determined by the BCCR. Repos and outright loans with a maximum maturity of 30 days³⁰ may be traded in this system. Settlement is gross, in real-time, and takes place through the reserve accounts the banks maintain at the BCCR.

Foreign currency trades are executed bilaterally using the MONED system, operated also by the BNV. Only spot trades are performed and settlement occurs on a payment versus payment (PvP)

²⁷ Article 10 of the SML. These securities may also be negotiated at the stock exchange if their maturity is less than 360 days.

²⁸ In Costa Rica repos are actually known as "repurchases" (*recompras*). Repurchases are a particular type of repo in which the underlying securities are deposited as collateral in a trust account created for this specific purpose and managed by the BNV. Throughout the rest of the Report the term "repo" will be used to refer to repurchases as they are known in Costa Rica.

²⁹ However, for the settlement of the securities leg the banks still require the custody services provided by the *Puestos de Bolsa*. For more details see Chapters 5 and 6.

³⁰ Article 11 of the Regulations of the Interbank Money Market.

basis. As indicated in the Regulations for foreign currencies trading through the MONED, the BCCR regulates and controls the clearance and settlement system of the foreign exchange market. Starting November 1998 transactions are settled gross and in real-time through the SINPE.

1.5 MAJOR TRENDS IN PAYMENT SYSTEMS

In recent years, important efforts have been carried out to increase the efficiency and safety of the payments system in Costa Rica, both for high value and for retail transactions. The most important initiative was the development of a global payments system called *Sistema Interbancario de Negociación y Pagos Electrónicos* (SINPE). The SINPE was developed by the BCCR in consultation with a great variety of market participants. Presently the SINPE is operated by the BCCR and all transactions are settled through the reserve accounts participants keep at the BCCR. The funds kept in these accounts are used both as the basis and collateral for payments and securities clearance and settlement operations. The BCCR provides reserve accounts for system participants both in local currency (colones) and in USD.

One of the most relevant innovations was the introduction of the “Customer Account” (*Cuenta Cliente*, CC) or “financial address”, which constituted the basis for the development of more efficient systems for collection and payment among financial entities. The definition of the CC represented one of the key elements of the financial and technological platform developed with the SINPE to offer new easier and safer services to the financial services users. The CC consists of the standardization of all checking and savings accounts of all financial institutions in the country, so that payment and collection transactions may be executed in any account at any financial institution in a rapid and precise way, thereby reducing costs and risks. The CC is comprised of 17 digits. The first 3 from left to right correspond to the code of the participating institution (assigned by the BCCR). Then, the following 13 digits are defined by financial institutions and are used to identify aspects such as the branch, the product (checking or savings account), currency (USD or colones) and the client itself. Finally, the last number to the right represents the verifying digit, which results from applying a mathematical algorithm to the previous digits in order to achieve information quality to guarantee the validity of the CC and decrease the risk of introducing wrong CCs into the system.

Every financial institution in the country may access the SINPE. Currently there are approximately 65 participating institutions which includes all banks (private and State-owned), several *Puestos de Bolsa* (brokers-dealers), all non-banking financial entities (entities that perform financial intermediation although without collecting sight deposits from the public), all mutuals (entities specialized in mortgage loans) and the biggest savings and loans cooperatives which represent 95 percent of the accounts of the cooperative sector. Other non-financial public institutions are also connected to the SINPE such as the Ministry of Finance (MH), the Social Security Institute (*Caja Costarricense del Seguro Social*, CCSS) and the State-owned insurance institute (*Instituto Nacional de Seguros*, INS).

One of the fundamental functions of the BCCR is its role as cashier for the Government. Thus, through the MH’s connection all payment transactions of the Central Government such as payrolls, suppliers, transfers to other public institutions, etc. are executed through the SINPE. On the other

hand the SINPE also provides a service for tax collection. Taxes paid at banks are automatically credited to the MH's account. Finally, at the end of 2001 an automated mechanism for tax declaration was implemented. Taxpayers may access the MH's web site to input the relevant information and payment, if any, is executed through the Direct Debit service of the SINPE.

The BCCR established that all entities holding a reserve account at the central bank must be connected to the SINPE so that all transactional relations with the BCCR be done electronically and executed by the entities themselves. Therefore, all manual procedures have been eliminated. Neither cheques, nor faxes or letters are used to move funds at the BCCR.

The SINPE started with a multilateral net deferred payment system, specifically for the automated clearance and settlement of cheques. This first centralized service is known as the Clearinghouse for Cheques and Other Securities (*Cámara de Compensación y Liquidación de Cheques y otros Valores*, CLC). The facility requires full standardization of physical cheques and electronic validation prior to the transmission of the corresponding file.

It is important to notice that the BCCR has the legal power to define the timing in which the crediting of funds stemming from payment transactions executed through the SINPE to end beneficiaries must occur. In this regard, the T + 1 period established for final settlement of funds at the clients' accounts has been a major improvement. Before, the crediting process at this level could take up to 15 working days.³¹

At present cheque truncation does not exist. However, some interbank commissions are discussing the issue and it is expected that by the beginning of 2003 the mechanism will be in place. Another step that has been taken to further improve the CLC is the standardization of the "Other Securities" that can be settled through the CLC, such as Term Deposit Certificates and Bills of Exchange.

Regarding high value systems, the most important initiative was the implementation of a real time gross settlement (RTGS) system within the SINPE. Through the system, known as "Electronic Funds Transfer" (*Transferencia Electrónica de Fondos*, TEF), a variety of transactions are settled such as monetary policy operations, transfers among financial institutions and among third parties, treasury payments, the cash leg of interbank money market transactions and foreign exchange transactions, and the net balances of deferred settlement systems. The cash leg of securities transactions executed through the MIB trading platform is settled gross on a Delivery versus Payment (DvP) basis (model 1 of the BIS classification).³² Foreign exchange transactions executed through the MONED system are settled on Payment versus Payment (PvP) basis. Participants have real time access to information on their reserve account at the BCCR, which enables them to monitor their balance, the history of their transactions, their compliance with legal reserve requirements, etc.

³¹ The great majority of cheques (99 percent) are processed by T + 1. However, cheques exchanged outside the San Jose metro area must be sent to the central clearing house and are processed no later than on T + 3.

³² "Delivery-versus-Payment in Securities Settlement Systems", Committee on Payment and Settlement System of the Central Banks of the Group of Ten Countries, Bank for International Settlements, September 1992.

Recent figures show that the daily average volume of transactions executed through the TEF is steadily increasing. In terms of total value settled (defined as the sum of the gross daily average value of processed payments), in year 2001 the TEF and the cheque clearing house (CLC) were similar. This demonstrates the relative importance the TEF system has been gaining versus the CLC.

In 2001 three new services began to operate within the SINPE: Tax Information and Settlement, Direct Credits and Direct Debits.

The Tax Information and Settlement service (*Información y Liquidación de Impuestos, ILI*) improves the BCCR's role as cashier for the Government. Before its launch, the BCCR had to gather all tax payments collected by authorized entities and then transfer them to the Government General Fund or to individual public entities in case of specific taxes. With the ILI services the MH's Treasury can access tax revenues one day after these were collected by financial entities. Settlement occurs at 2.00 p.m. on the same day in which files are sent to the ILI (T + 1). Additionally, the MH has access to real-time information on its account.

The Direct Credits service (CCD) was welcomed by financial entities right after its implementation. After eight months of operation the service grew more than 4 times. The average value of a transaction in this period was of about ₡92,000 (equal to USD 280). Until today, the BCCR and the MH are the heaviest users of the CCD service. Domestic firms are expected to begin using the service to pay their employees and suppliers shortly.

The Direct Debits service (CDD) has been in use since December 2001. Volume is still low since financial institutions are still in the stage of adapting their own systems and marketing this service to their clients. As the experience in other countries suggests, it is expected that once the CDD service is known better, the public will start using it massively.

Currently the BCCR is carrying out an advertising campaign to inform the citizens on the advantages of the new electronic payment instruments available in the market through the SINPE.

Another service operating since February 2002 is the Settlement of External Services (*Liquidación de Servicios Externos, LSE*). The system currently settles the net positions stemming from the clearing of the country's largest ATM network, ATH. This service settles bilateral transactions that are electronically transmitted to the SINPE by an associate entity in charge of a clearinghouse. The LSE is capable of handling the settlement for more than one of these clearinghouses. It is expected that the service will also be used shortly by the BNV and other retail payment markets such as credit and debit card transactions.

Regarding cross-border payments, in the second semester of 2001 the BCCR changed the payment mechanism when it hired SWIFT services. Previously, funds transfers from/to other countries were handled through the private networks of two correspondent banks of the BCCR: Citibank and the BICSA network. With the new framework the possibilities for executing payments with financial institutions all over the world have been expanded.

Regarding the costs of using the SINPE, the pricing policy stems from the LOBCCR, which states that the BCCR must recover both the investment costs and the expenses incurred in developing the

system. A pricing model was developed accordingly and it is based on a fixed tariff (monthly fee) for every single service, a variable cost for each transaction executed through the system and a charge for each terminal connected to the SINPE. The model has been accepted by participating institutions. The MH in particular has already reported significant savings in fees and related charges when compared to its situation prior to the introduction of the SINPE. The BCCR is also promoting a pricing model in which participants agree among themselves on the fees the destination entities will charge to the originating entities for each received transaction. An agreement has already been reached for the Electronic Funds Transfer, Direct Credits and Direct Debits systems.

1.6 MAJOR TRENDS IN SECURITIES CLEARANCE AND SETTLEMENT SYSTEMS

Securities are represented by means of physical certificates or immobilized at the central securities depository (CSD). The “*Central de Valores de la Bolsa Nacional de Valores, S.A.*” (CEVAL) is a private firm whose only owner is the BNV. Brokers-dealers, banks and pension funds may participate directly in CEVAL, although the last two have only non-operational custody accounts.³³

As of May 2001, 68 percent of the debt securities and 53 percent of stocks were immobilized. Meanwhile, 98 percent of international bonds and 100 percent of international stocks were immobilized. Full dematerialization of securities is possible according to the SML.³⁴ However, at the time this Report was drafted no dematerialized issues had been made. So far, immobilized global notes are being used as a means to facilitate securities trading and settlement. The Government still issues physical bonds and approximately 40 percent of its total outstanding debt is not yet immobilized.

A standardization process for securities is currently taking place. The SML states that in order for an issue of securities to be offered publicly in the primary market it must be serialized and must comply with other requirements set by the SUGEVAL.³⁵ There is also a project to assign identification numbers compatible with the International Securities Industry Numbering (ISIN) standards.

Regarding securities clearance and settlement, the SML states that the settlement of transactions carried out in the organized markets must be executed through the securities clearance and settlement system, which will be integrated by the stock exchanges and by clearance and settlement firms (*sociedades de compensación y liquidación*).³⁶ Except for the MIB, which follows real time gross settlement, the trading systems of the stock exchange settle transactions in a fashion similar to that of Model 2 of Delivery versus Payment (DvP) of the Bank for International Settlements (BIS).³⁷ The CEVAL acts as the settlement agent for the securities leg, which is settled gross on the brokers-

³³ The securities in these accounts can only be traded if they are transferred to the account of a broker-dealer or to that of the MIB for the interbank money market.

³⁴ Article 115 of the SML.

³⁵ Article 10 of the SML. According to Article 10 of the SML, individual issues of debt securities made by entities regulated by the SUGEVAL are exempt of this requirement.

³⁶ Article 126 of the SML.

³⁷ “*Delivery-versus-Payment in Securities Settlement Systems*”, Committee on Payment and Settlement System of the Central Banks of the Group of Ten Countries, Bank for International Settlements, September 1992.

dealers' accounts. As for the cash-leg, the clearing system of the stock exchange calculates a single multilateral net position for the transactions executed in all four trading systems, and settlement occurs at the reserve accounts intermediaries hold at the BCCR.³⁸

For none of the trading systems the clearance and settlement system act as a central counterparty. On the other hand, although the systems of the BNV and of CEVAL are interconnected to each other, they are not interconnected to the BCCR system. Thus, securities and cash are settled separately under imperfect DvP procedures.

Accordingly, it can be said that securities markets in Costa Rica are fragmented and that the majority of transactions are not settled under a true DvP environment. Moreover, risk controls for the multilateral net positions by which the cash leg is settled appear to be insufficient³⁹ to support the system in the event of a default. In such a case, the ultimate procedure would be to unwind and recalculate the net positions.

Considering the above, the relevant authorities are working on a project aimed at improving the current clearance and settlement system. The project, know as Book Entry System (*Sistema de Anotación en Cuenta, SAC*), is at an advanced stage of development.

Among its main features the SAC will have an open architecture that, in principle, will allow the operation of all kinds of securities. Both brokers-dealers and banks will be able to open fully operational accounts both for themselves and for their clients. The new system will have two separate DvP mechanisms, one for the net settlement of transactions executed through the BNV (DvP Model 2) and the other for the real time gross settlement of interbank money market transactions (DvP Model 1). To ensure a true DvP for both cases the SAC will be connected to the RTGS system of the SINPE.⁴⁰ Finally, prior to becoming operational the SAC will have a settlement fund, to be created and managed by the BNV, and other similar risk management mechanisms in order to guarantee the settlement of multilateral net positions stemming from stock exchange transactions.

³⁸ The use of the reserve accounts in the BCCR as a settlement asset for securities transactions started in August 2000.

³⁹ In the BNV there's a guarantee fund of \$5 million (approximately USD 15,000 according to the exchange rate prevailing at the end of June of 2001) per broker-dealer.

⁴⁰ This system is called Interbank Settlement System (*Sistema Interbancario de Liquidación, SIL*).

2 INSTITUTIONAL ASPECTS

2.1 GENERAL LEGAL FRAMEWORK

With the strengthening of the economic and banking activity in the country, the need arose to review the role and purpose of the Central Bank. The Central Bank developed from the simple Issuing Department that until that moment (1945) was functioning within the *Banco Nacional de Costa Rica*. In 1948, once private banks were nationalized,⁴¹ it became more urgent to establish the Central Bank as an independent organization with responsibilities over the credit, economic and monetary policies of the country. For this purpose Law 1130 of 1950 was enacted, giving the *Banco Central de Costa Rica* (BCCR) its own and defined characteristics.

This Law 1130 was transitory and the BCCR would initially have the same functions and powers of the Issuing Department until the disappearance of the latter. In 1953 Law 1552, called the Organic Law of the Central Bank of Costa Rica (LOBCCR), was enacted. This was later replaced by a new LOBCCR, Law 7558 of 1995, which is ruling at present.

In Costa Rica, the official regulatory and supervisory organizations of the financial systems (SUGEF, SUGEVAL and SUPEN) are affiliated to the BCCR under a regime of autarchy.⁴² With the enactment of the Securities Market Law (SML), Law 7732 of 1998, the *Consejo Nacional de Supervisión del Sistema Financiero* (CONASSIF)⁴³ was created. CONASSIF is an “umbrella” that seeks uniformity and integration in the regulation and supervision of the financial system in Costa Rica.

The SML granted the CONASSIF the sole regulating or ruling power over the supervised financial sector. Thus, the powers previously vested in the Boards of Directors of the three supervisory agencies were unified in CONASSIF. Therefore, CONASSIF is the institution responsible for issuing all regulations for the financial system as well as the general policies that govern the three superintendencies of the financial system (for more details, see section 2.6.1).

Table 6 contains the principal laws that govern Costa Rica’s financial activities.

2.1.1 Payments

As stated in Articles 2, 3, 68 and 69 of the LOBCCR, the BCCR has responsibility for the payments system. Article 69 is specific about the organization of the payments system. It states that the Board of Directors of the BCCR will organize and regulate the functioning of the payments system. However, this Article is not totally clear about the scope of the BCCR regarding supervision and control of private payment systems and of the role of SUGEF in this field.

⁴¹ “Nationalization” here refers to the exclusivity granted to the State to receive deposits from the public.

⁴² Autarchy is defined in the Public Administration General Law of 1978. “Autarchy” refers to the impossibility of the superior to influence the inferior’s faculties and revise its behavior. In addition to this, “maximum autarchy” also states that the inferior is not compelled to comply with the orders, official communications or instructions of the superior.

⁴³ Article 169 of the Law 7732.

Table 6: Legal Framework of the Financial System in Costa Rica

Law No.	Name (free translation)	Ruling since
1644	Organic Law of the National Banking System (<i>Ley Orgánica del Sistema Bancario Nacional</i>).	27/09/53
4179	Law of Cooperative Associations and Creation of the National Institute for Cooperative Promotion (<i>Ley de Asociaciones Cooperativas y creación del Instituto Nacional de Fomento Cooperativo</i>)	29/08/68
4351	Organic Law of the Popular and Community Development Bank (<i>Ley Orgánica del Banco Popular y de Desarrollo Comunal</i>)	19/07/69
4631	Net Income Due to Acquisition of Auctioned Goods (<i>Utilidades Netas por Venta de Bienes Adjudicados en Remate</i>)	23/08/70
5044	Law for the Regulation of Non-Banking Financial Firms (<i>Ley de Regulación de Empresas Financieras No Bancarias</i>)	05/11/72
7052	Law of the National Financial System for Housing (<i>Ley del Sistema Financiero Nacional para la Vivienda</i>)	27/09/86
7107	Law for the Modernization of the Nation's Financial System (<i>Ley de Modernización del Sistema Financiero de la República</i>)	22/11/88
7391	Law for the Regulation of the Financial Intermediation Activities of Cooperatives (<i>Ley de Regulación de la Actividad de Intermediación Financiera de las Organizaciones Cooperativas</i>)	24/05/94
7523	Private Complementary Pensions Regime and Reforms to the Securities Market Law and Commerce Code (<i>Régimen Privado de Pensiones Complementarias y Reformas de la Ley Reguladora del Mercado de Valores y del Código de Comercio</i>)	18/08/95
7558	Organic Law of Central Bank of Costa Rica (<i>Ley Orgánica del Banco Central de Costa Rica</i>)	27/11/95
7732	Securities Market Law (<i>Ley Reguladora del Mercado de Valores</i>)	27/01/98
7983	Law for the Protection of Workers (<i>Ley de Protección al Trabajador</i>)	18/02/00
8204	Law on Narcotics, Psychotropic Substances, Non-Authorized Drugs, Capital Legitimate Sources and Connected Activities (<i>Ley sobre Estupefacientes, Sustancias Psicotrópicas, Drogas de Uso No Autorizado, Legitimación de Capitales y Actividades Conexas</i>)	10/01/02

Source: SUGEF.

The current interpretation, consistent with the general practice in most countries, is that the BCCR has the responsibility for regulating, organizing and overseeing its own payment system (SINPE) as well as overseeing the self-regulatory private systems in order to provide customers with a continuous, timely, efficient and safe financial services in an environment of free access and competition for all the participants. Moreover, SUGEF supervises and controls the compliance with regulations by all participants as well as their own particular financial health.

In order to clarify the powers and faculties of each of these institutions as well to include other issues that currently are not explicitly stated, several changes in this regard have been included in the LOBCCR reform project. Cheques are regulated by the provisions contained in the Civil and Commercial Codes (see Section 3.2.1).⁴⁴

⁴⁴ The legal framework for cards is described in Section 3.2.3.1.

2.1.2 Securities

The Securities Market Law (SML), Law 7732 of 1998, is the framework rule in force for the securities market. It regulates the persons or firms that participate either directly or indirectly in it, the actions, contracts and securities related to these markets and the Securities Regulator (*Superintendencia General de Valores*, SUGEVAL).⁴⁵ Moreover, in Article 4 the SML establishes that the Central Government and all other public sector institutions will have to consult SUGEVAL before issuing any act of general application related to the securities market.

In Article 2 securities are defined as the certificates and any other economic or property right, included or not in a document, that because of its own legal configuration and transfer regime may be traded in a financial or stock market. This same Article defines a public offering of securities as an offer, implicit or explicit, with the intent of issuing, placing, negotiating or trading securities being transmitted by any media to the general public or to particular groups. A public offer of securities may be made only by those entities authorized by the SUGEVAL. Later on, Article 10 states that only those securities issued in series and authorized by SUGEVAL may be publicly offered in the primary market.

Regarding the secondary markets, the law establishes that these will be organized by the stock exchanges, which must be authorized by SUGEVAL, and that only the securities issuances registered in the Securities and Intermediaries National Registry (*Registro Nacional de Valores e Intermediarios*, RNV) ⁴⁶ may be traded or publicly offered in these markets. The buying, selling and repos of publicly offered securities must be executed through the members of the stock exchanges, which must be the property of the *Puestos de Bolsa* (brokers-dealers) participating in them.⁴⁷

Title VII deals with the clearance, settlement and custody of the securities. Article 115 states that the securities issuances registered in the RNV may be represented by means of electronic book entries or with paper certificates, the first of which is irreversible.⁴⁸ Chapter I of the same Title (Articles 115 to 125) establishes a special regime for the dematerialized issues, regulating aspects such as the entities that may perform the functions of a central securities depository (CSD), investors' rights, securities transfers and the creation of liens on this kind of securities.

The book entry system is currently being developed by the BCCR⁴⁹ and the SUGEVAL. For this purpose the Regulation on Securities Public Offerings of September 1999 establishes a transition period in which securities issues may be represented by global notes.⁵⁰

⁴⁵ For more details regarding SUGEVAL functions, see Section 2.8.

⁴⁶ Article 22 of the Law 7732 (SML).

⁴⁷ Articles 23 and 27 of the Law 7732 (SML), respectively.

⁴⁸ The transitory Article VII of the SML states that the CONASSIF may establish that securities being represented by means of electronic book entries become mandatory.

⁴⁹ Article 117 of the SML gives the BCCR the responsibility of managing the issuance registries of the State and the public institutions, being capable of delegating this function to some entities belonging to the National Book Entry System. The responsibility for managing the issuance registry of private issuers is given to the CSDs authorized by the SUGEVAL.

⁵⁰ Transitory Article VIII of the Regulations of the Securities Public Offerings.

The obligation for standardization of securities issues stated in Article 10 of the SML implies that all securities within an issue have the same characteristics in terms of face value, terms and maturity. The specific guidelines for standardization are established in the Regulation on Securities Public Offerings.

The legal background of the securities clearance and settlement system is found in Articles 126 to 133 of the SML. The system comprises the stock exchanges and clearance and settlement firms. All transactions executed in the organized markets must be settled through this system. The system will provide for the generalization of the electronic book entry system, following the principles of universality, delivery versus payment, guarantee of delivery and financial neutrality. The system will also have to establish mechanisms to ensure that payment will be made in those cases in which participants lack the necessary funds, through the use of the collateral systems to be established by SUGEVAL.

Brokers-dealers, banks and the public institutions that comply with the requirements established by SUGEVAL may become settlement agents and shareholders of the clearance and settlement firms. CSDs are explicitly empowered to provide clearance and settlement services.

CSDs must be authorized by SUGEVAL. Article 134 of the SML gives them also the possibility, together with brokers-dealers and entities subject to SUGEVAL control, to offer custody services, including the administration of economic rights associated with the securities under custody. Articles 119 and 134 to 143 regulate different aspects of the central depository and custody functions such as the constitution of a deposit, proof issuance, restitution of securities, bonds or documents and depositor protection in case of bankruptcy or insolvency of a custodian.

In August 1994, the only CSD in Costa Rica, the *Central de Valores de la Bolsa Nacional de Valores S.A.* (CEVAL), was created. Its equity is totally owned by the BNV.⁵¹ Currently CEVAL administrates and performs the clearance and settlement of the securities deposited in it. It also issues “pledge certificates” (*cédulas prendarias*) and administrates multiple or global notes associated with deposited securities. The regulations of the BNV establish the main characteristics of the CEVAL. Meanwhile, CEVAL’s own regulations specify the features of the registry system, types of depositors, their requirements and obligations, the services being offered, including the clearance and settlement of the transactions executed at the BNV, its obligations towards depositors and the termination clause for deposit contracts, among others.

It is expected that once the Book Entry System (*Sistema de Anotación en Cuenta, SAC*) is in place, the private entity being delegated by the BCCR to run the system will become a new CSD.

2.1.3 Derivatives

The derivatives market is very incipient. The former National Securities Commission (*Comisión Nacional de Valores*), antecessor of the SUGEVAL, issued a regulation for the futures market organized

⁵¹ The SML of 1998 establishes in its Article 119, sub-section 3 that the stock exchange will be able to have a stake in the capital of a CSD (for a maximum of 40 percent). Therefore, the new central securities depository that will arise as a consequence of the implementation of the Book Entry System will allow the stock exchange to participate with a maximum of 40 percent in its capital with the remaining 60 percent equally distributed among the rest of its participants.

by stock exchanges based on what was established at that time in Law 7201, the SML of 1990. This Law gave powers to the Commission to promote, authorize, regulate and control futures, options and other derivatives that could be developed in the country.

The SML of 1998 mentions several very specific issues related to this market. In Article 43, in Section 4 that deals with stock exchange contracts, it states that futures market transactions are to be paid on the day specified in the contract and that all of them will expire on the same day. The regulations of the stock exchange will set the margin requirements participants will have to deposit with the brokers-dealers in order to trade futures contracts and maintain their positions. Regarding settlement, Article 128 determines that the SUGEVAL is empowered to authorize and regulate the settlement of derivatives market transactions.

So far, the efforts to develop a derivatives market, particularly that of interest rate futures, have not been effective in terms of market development and trading volume.

2.1.4 Specific Legal Issues Related to Clearance and Settlement

2.1.4.1 Netting

Neither the Civil and Commercial Code nor the SML have explicit rules for netting agreements (either bilateral or multilateral). Article 130 of the SML implicitly recognizes this arrangement for securities clearance and settlement. However, in case of an insolvency the decision would rest on a general judicial court. Netting principles are little known in sectors other than payments and securities clearance and settlement.

2.1.4.2 Settlement Finality

There is no explicit mention in any Law on when settlement becomes final.

2.1.4.3 Zero Hour Rule

The Costa Rican laws do not contain a zero hour rule that invalidates transactions already settled and considered final which were executed since the beginning of the day in which a bankruptcy occurs. In case of an insolvency retroactive effects could be possible only if transactions seem to be of a fraudulent nature or if they are considered unfair and harmful for the rest of the creditors (*Actio Pauliana*). Even so, for pending transactions it is not clear whether settlement will occur when and if a bankruptcy occurs.

2.1.4.4 Digital Documents and Signatures

The SML in its Article 180 recognizes electronic or magnetic transmission and data storage media used by the SUGEVAL, the SUGEF and the SUPEN as official proof in a court of law. Their validity is equivalent to that of paper documents for all legal purposes.

The Government is presently discussing a more specific project, the Law on Digital Signatures and Digital Certificates (*Ley de Firma Digital y Certificados Digitales*). This project aims at regulating

and giving legal recognition to digital signatures and to authorize its use by the Government. This will have the same legal validity and effectiveness to that of written signatures or others by which a will to engage in any relation is expressed.

2.1.4.5 Novation

Although the SML includes a section that deals with the clearance, settlement and custody of securities, there is no mention on novation.⁵²

Nonetheless, the Civil Code contains a chapter about novation. From Articles 814 to 820 the Code states the conditions under which novation may be executed and several specific rules for its operation. Among these, a particularly relevant one is that novation should be voluntarily and explicitly agreed upon by the parties.

2.2 THE ROLE OF FINANCIAL INSTITUTIONS: PAYMENTS

2.2.1 The Banking Sector

Currently the commercial banking system is comprised of 3 State-owned banks, 16 private banks and 2 banks created by special laws.⁵³ All these institutions are connected to the SINPE.

Of the laws governing the banking system, the LOBCCR and the LOSBN are the most relevant ones. Additionally, banking entities are subject to the rules issued by the SUGEF and the CONASSIF.

With the 1995 reform, the private banks in particular increased the number of financial products being offered to their clients. Thus, in recent years the banking sector has become more dynamic and competitive, despite a clear dominance of the State-owned banks.

2.2.2 Other Institutions that Provide Payment Services

Besides the commercial banks, other institutions performing financial intermediation and which are connected to the SINPE are the non-banking financial entities, the mutuals and the savings and loans cooperatives.

These entities are supervised and controlled by the SUGEF. The non-banking financial entities are known as "*financieras*". Under this legal category firms may perform any financial intermediation activity except for those that the law confers exclusively to commercial banks, such as chequing or savings accounts deposits. These entities are regulated by the Law for the Regulation of Non-Banking

⁵² According to the BIS "Glossary of terms used in payment and settlement systems", novation is the satisfaction and discharge of existing contractual obligations by means of their replacement by new obligations.

⁵³ The banks created by special laws are: the *Banco Hipotecario de la Vivienda* (BANVHI – 1986) and the *Banco Popular y de Desarrollo Comunal* (1968). The first is the main entity for the financing of housing while the second was created for the economic protection of the workers and to stimulate community development through the financing of particular projects.

Financial Firms (*Ley de Regulación de Empresas Financieras no Bancarias*), Law 5044 of September 1975, and its reforms.

The savings and loans “mutuals” (“*mutuales*”) were created to foster savings in order to finance housing. Mutuals may take deposits in savings accounts and through investment certificates and they may only grant loans for housing.⁵⁴ The resources collected by the *financieras* and *mutuales* are subject to the minimum legal reserve requirement. For this reason, they keep reserve accounts with the BCCR and need to be connected to the SINPE.

The savings and loans cooperatives are voluntary associations of persons, not firms. Cooperatives have their own legal standing, limited responsibility and their duration is unlimited. These entities may take deposits for savings or term accounts but not for chequing accounts. The activities and nature of the cooperatives are defined in the Law of Cooperative Associations, Law 4179 of 1968, and its modifications.

Through a CONASSIF agreement, cooperatives performing financial transactions with non-associates and whose net assets as of December of each year are equal to or bigger than ₡300.0 million are subject to the reserve requirement. All other cooperatives are subject to the liquidity reserve requirement.⁵⁵

Finally, there are also some card operators, whose role is described in Chapter 3.

2.3 THE ROLE OF FINANCIAL INSTITUTIONS: SECURITIES

2.3.1 Securities Market Participants

The main participants in the Costa Rican securities market are the following:

Issuers

Public or private sector companies who have their securities registered in the RNV.

Securities Intermediaries

The SML of 1998 establishes in its Article 23 that the buying, selling and repos of publicly offered securities must be executed through the members of the stock exchange, which, according to Article 27, are the *Puestos de Bolsa*. The activities of a *Puesto de Bolsa* are limited to those authorized by the SML (Article 56) and those authorized by SUGEVAL's regulation. The National Insurance Institute (*Instituto Nacional de Seguros*) and State-owned banks are also authorized to create subsidiaries with the sole purpose of operating their own broker-dealer.⁵⁶

⁵⁴ For further information regarding the National Financial System for Housing see Law N. 7052 of November 13, 1986, and its modifications.

⁵⁵ See Section 1.3. However, all cooperatives are authorized to perform financial intermediation.

⁵⁶ Article 55 of the Law N. 7732.

Stock Exchange Agents

Individuals who represent a broker-dealer. They hold a license granted by the stock exchange and may execute transactions with the clients on behalf of the broker-dealer.

Institutional Investors

This group of investors is comprised of the complementary pension funds handled by the Complementary Pension Plans Managing Firms (*Operadoras de Planes de Pensiones Complementarias*, OPCs), investment funds managed by Investment Funds Managing Firms (*Sociedades Administradoras de Fondos de Inversión*) and the fiduciary funds managed by banks or entities under the control of SUGEF.

Risk Rating Agencies

Firms whose exclusive role is to rate the risks of the securities registered in the RNVI. According to Article 144 of the SML all debt issues must be rated, except for those of the Government and those of public non-banking institutions. Currently there are two rating agencies in Costa Rica authorized by CEVAL: SCR *Costa Rica Calificadora de Riesgo, S.A. Duff & Phelps* and SCR *Sociedad Clasificadora de Riesgo, S.A.*

Central Securities Depositories

CSDs are entities providing the service of custody for securities and the management of economic and property rights related to the securities in custody. CSDs must receive prior authorization from SUGEVAL. Moreover, they can be authorized by SUGEVAL to provide clearance and settlement services for securities transactions executed at the stock exchange. At present CEVAL is the only CSD functioning in Costa Rica.

Clearance and Settlement Firms

The function of these companies is to settle transactions made in the organized markets. The brokers-dealers, the banks and the public institutions can become settlement agents and shareholders of these companies if they comply with the requirements established by SUGEVAL for this purpose.

2.3.2 Exchanges

Stock exchanges are owned by the brokers-dealers that participate in it. The share of an individual broker is limited to 20 percent of the stock exchange's equity. According to Article 27 of the SML, the sole function of stock exchanges is to facilitate securities transactions and, according to the powers conferred to them by the same law, to authorize, control and regulate the brokers-dealers and their agents.

Stock exchanges are subject to the SUGEVAL's prior approval. Among the established requirements by the SML for authorization is that at any moment the minimum subscribed and paid in capital must be ₡200 million.

Until January of 1999 both the BNV and the Electronic Stock Exchange were operating in Costa Rica. Starting from this date, and as a result of a merger, the BNV became the only stock exchange operating in the country. The value traded at the BNV during year 2000 reached \$8,263,314 million, including primary and secondary market operations, the latter representing 73.5 percent of the total. Transactions with public debt securities represented 92 percent of the total value traded and those of the stock market merely 0.4 percent. In March 2000 market capitalization was \$717,154 million.

2.3.3 Securities Clearance and Settlement Institutions

Presently, the clearing and settlement of transactions made at the stock exchange is done through the CEVAL and the reserve accounts in the BCCR. CEVAL does not act as central counterparty and its system is not interconnected with the SINPE. Once the Book Entry System (SAC) is in place this could become the new CSD and its system would be connected to the SINPE.

Transactions at the OTC market are settled bilaterally among the parties. Settlement of the securities leg occurs through the physical delivery of securities or transfers in CEVAL's accounts, while the cash leg is settled with a cheque or by means of electronic transfers.

2.4 MARKET STRUCTURE AND REGULATION

In Costa Rica, the securities market almost totally consists of operations executed through the BNV trading platforms. The OTC market is not very relevant and trading in it is limited to some individual debt securities issued by entities supervised by the SUGEF.

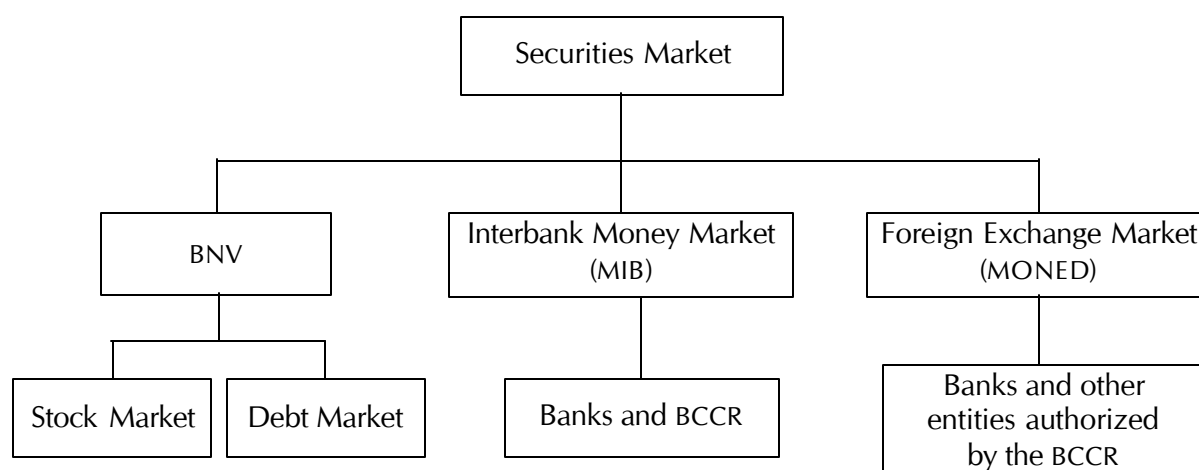
Interbank money market transactions are made through the MIB system in which only the BCCR and banks may participate. On the other hand, foreign exchange transactions are executed bilaterally through the MONED system. Both the MID and the MONED are operated by the BNV.

The situation in the money market is currently changing from a dominating position of brokers-dealers to one in which banks are becoming the major players.⁵⁷ The brokers-dealers are authorized to operate accounts similar to investment funds (OPABs and CAVs⁵⁸) with the public, which allows them to be active participants in the money market.

SUGEVAL is charged with the regulation, supervision and control of the securities markets. However, its powers are limited by the SML, which confers to the CONASSIF the powers to dictate the rules for

⁵⁷ To understand the present situation it must be remembered that until the mid-Nineties private banks were not allowed to take deposits for current accounts. This activity was a monopoly of the State-owned banks.

⁵⁸ The Stock Market Management Transactions (*Operaciones de Administración Bursátil*, OPABs) and the Securities Administration Accounts (*Cuentas de Administración de Valores*, CAVs) are securities portfolios managed by the brokers-dealers for short-term investment purposes. The maximum maturity of the portfolio is 182 days, although up to 30 percent of the portfolio may be invested in 6 or 12 months securities as long as these are standardized and have sufficient liquidity according to SUGEVAL's opinion. These investment instruments are expected to disappear by 2003.

Figure 1: Market Structure

Source: Prepared with information provided by the SUGEVAL.

authorization, regulation, supervision, control, and surveillance that SUGEVAL and the other supervisory agencies must execute. In this regard, SUGEVAL may propose new regulations to the CONASSIF. SUGEVAL would then be in charge of executing the decisions issued by the latter.

2.5 THE ROLE OF THE CENTRAL BANK

2.5.1 Monetary and Foreign Exchange Policies

The LOBCCR establishes the objectives and functions the central bank must follow in relation to monetary policy. Article 2 of this law sets the general objectives of the BCCR and among them it states that the BCCR should avoid or otherwise contain price fluctuations originated in the credit and money markets, which is the primary purpose of the monetary policy.

Other functions of the BCCR are defined in Article 3. The Monetary Authority must preserve the stability of the external value of the currency and its convertibility, define and manage the monetary and foreign exchange policies, issue bills and coins according to the real needs of the economy and act as a custodian of the legal reserve requirements constituted by financial intermediaries.

In order to fulfill objects and functions, the BCCR may use direct as well as indirect monetary policy instruments according to what is established in Chapter II "Monetary, Financial and Exchange Policies" of the LOBCCR as well as in the Monetary Policy Regulations of February 16, 1996. The monetary policy instruments may be classified in: i) Credit facilities; ii) Deposits and other liabilities; iii) Foreign exchange policy instruments; and, iv) Temporary instruments.

2.5.2 Involvement in the Payments System

Besides its traditional objectives, in the payment area the BCCR fulfills the objectives and functions established in the LOBCCR and in the regulations for the system, the most important being the Payments System Regulations (*Reglamento del Sistema de Pagos*).⁵⁹

⁵⁹ At present it's in force the Edition N. 6 of this Regulation of June 18, 2001

Article 2 of the LOBCCR states that one of the objectives of the central bank is to foster the efficiency of internal and external payments, the continuity of the payments system and the promotion of a stable, efficient and competitive financial intermediation system. Article 3 states that among its vital functions the BCCR is responsible for the implementation, operation and control of the clearance system. Article 69, which deals with the organization of the payments system, states that the Board of Directors of the BCCR is the entity charged with the organization of the payments system and of regulating its functioning.

According to the latter, the BCCR assumes the following specific roles: system developer, operator, regulator, overseer and participant.

2.6 THE ROLE OF THE SUPERVISORY AGENCIES OF THE FINANCIAL SYSTEM

2.6.1 CONASSIF

CONASSIF is responsible for issuing all regulations for the financial system as well as the overall policies that govern the three supervisory agencies of the financial system. In this regard, Article 169 of the SML states that the SUGEF, the SUGEVAL and the SUPEN will all function under the direction of the CONASSIF).

The members of CONASSIF are the Minister of Finance, the President or the General Manager of the BCCR and five representatives not holding public sector positions. The three Superintendents may participate in CONASSIF's meeting although with no voting rights.

The specific functions of the CONASSIF are described in Article 171 of the SML. Among these the most relevant are the following:

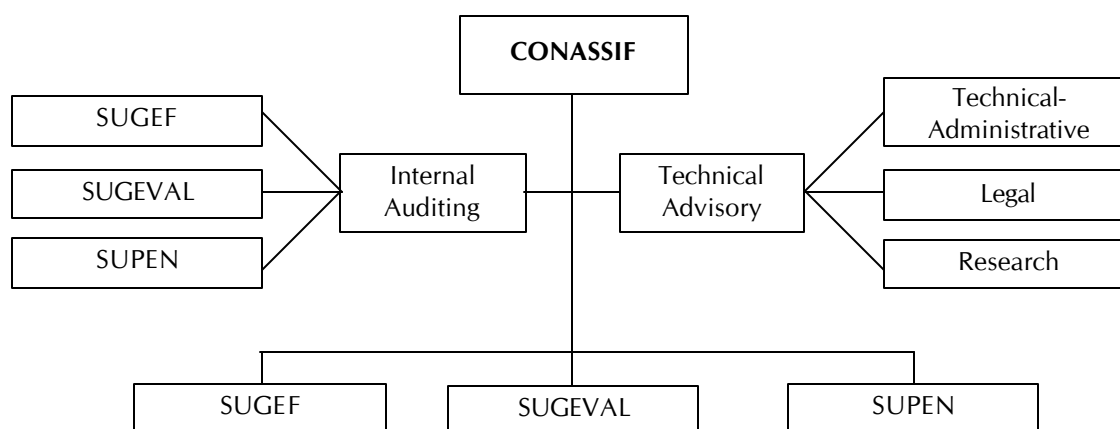
- Designate and dismiss the Superintendents, their Deputies, Auditors and the SUGEF's Internal Deputy Auditor.
- Dictate the rules regarding authorization, regulation, supervision, control and surveillance that, according to the law, the superintendencies must execute. Additionally, approve the rules by which persons and/or firms are to be considered as part of a single economic group.
- Approve the rules for accounting and auditing as well as the frequency of external audits and the disclosure of their outcome.
- Terminate the operations of any of the entities regulated by the superintendencies. Also, it may order the intervention of such entities and request their liquidation to the relevant authorities. Additionally, to suspend or revoke the authorization granted to such entities to make public offerings of securities.
- Be informed and make decisions on the appeals presented to it regarding complaints against resolutions of the superintendencies. Additionally, be informed of complaints against

resolutions of the stock exchanges regarding authorizations to brokers-dealers and sanctions to these as well as to stock exchange agents.

- f. Regulate information exchanges among superintendencies, approve their general organizational rules, operational plans and budgets and solve any jurisdiction conflicts that may rise.

The institutional model followed in Costa Rica for the supervision of the financial system is shown in the following figure:

Figure 2: Structure of the CONASSIF



Source: CONASSIF.

2.6.2 Role of the Banking Supervisory Authority

The *Superintendencia General de Entidades Financieras* (SUGEF) is an autonomous organization that functions under the umbrella of the BCCR. It was created in 1995 when the supervision of financial entities was declared as being of public interest in the new LOBCCR. The SUGEF's main role is the supervision and control of the entities that perform financial intermediation to enhance the transparency, stability, soundness and efficiency of the national financial system, thereby protecting the interests of the general public.

For many years the SUGEF actually functioned as a department within the BCCR. This was called the "Banks General Audit" (*Auditoria General de Bancos*, AGB). The LOBCCR of 1952 established that the AGB functions included the surveillance and control of all of the BCCR's departments and agencies, as well as those of other banking institutions in the country, including their branches and agencies, and any other entities considered by the law.

Later, with the introduction of the Law 7107, the Law for the Modernization of the Nation's Financial System (*Ley de Modernización del Sistema Financiero de la República*), the AGB was replaced by

the “Financial Entities General Audit” (*Auditoria General de Entidades Financieras*, AGEF), a maximum decentralization agency under the umbrella of the BCCR.⁶⁰ With this reform the AGEF controlled the functioning of all banks, including the BCCR, the non-banking financial companies and other public or private entities, whatever their legal nature, performing financial intermediation either directly or indirectly or any other services of a nature similar to that of banking.

The new LOBCCR grants the SUGEF more powers and autonomy. Some of the most relevant functions of the SUGEF according to the LOBCCR are the following:

- Watch over the stability, soundness and the efficient functioning of the national financial system.
- Supervise the operations and activities of the entities under its jurisdiction.
- Determine the general necessary rules for healthy banking practices to be established.
- Establish categories of financial intermediaries based on their type, size and level of risks being undertaken.
- Provide assistance to the controlled entities.
- Provide the Board of Directors of the BCCR with reports on its supervision and control activities.
- Fulfill any other function mandated to it by the law, regulations and others.

The SML in force since March 1998, introduced changes to Articles 121, 122 and 123 (abrogated), which dealt with SUGEF principals, its Board of Directors, organization and legal powers. The functions of the former Board of Directors of the SUGEF were transferred to the CONASSIF. The Superintendent of the SUGEF may attend CONASSIF’s meetings, although with no voting rights.

Supervised Entities

The following institutions are controlled by the SUGEF (and by the BCCR for monetary purposes): private and State-owned banks, banks created by special laws, non-banking financial firms, savings and loans mutuals, savings and loans cooperatives, foreign exchange houses and financial groups⁶¹

⁶⁰ Article 124 of the Law 1552.

⁶¹ A financial group gathers subsidiaries exclusively dedicated to the provision of financial services under the control and management of a single company or similar legal entity. Financial groups may be comprised by banks, non-banking financial firms, general warehouses, brokers-dealers, investment companies, leasing companies, factoring companies, insurance companies, complementary pension plans, banks and investment companies registered abroad credited for this by the correspondent foreign authority, and any other kind of firm dedicated exclusively to the provision of financial services and authorized for this purpose by the Board of Directors of the BCCR. Through the financial groups the SUGEF carries out an indirect supervision of the so-called offshore banks.

and any other entity authorized by law entity to perform financial intermediation.⁶² At present SUGEF supervises and controls about a hundred entities.

Supervision Model

The Law 7558 modifies the ex-post repressive supervision traditionally used by SUGEF for a model of ex-ante prudential supervision in which the main goals are to ensure transparency, improve the strength and foster the development of the nation's financial system. This model is based on the analysis of the financial quality of the supervised institutions for which a CAMELS⁶³ approach is used, reflecting the evaluation of each entity in a progressive numeric scale, from best to worst, from one to four.

The rules the SUGEF applies to controlled financial intermediaries are based on the recommendations issued by the Basel Committee on Banking Supervision of the Bank for International Settlements (BIS).

For supervisory purposes the SUGEF is internally organized in the following three areas, each one with its own on site and off site supervision departments:

- Savings and Loans Cooperatives and Financial Firms (*Financieras*).
- State-owned Banks and Savings and Loans Institutions.
- Private Banks and Financial Groups.

Every year two on site inspections are carried out for each controlled entity. The first is executed thoroughly and in-depth, while the second one is basically a follow up.

2.6.2.1 Oversight of the Payments System

Article 69 of the LOBCCR grants powers to SUGEF to control and oversee the clearinghouse established by the BCCR. However, in year 2001 the Board of Directors of the BCCR approved the creation of a new administrative structure specially designed to satisfy all the functions associated with the oversight of the payments system. A proposal to modify the LOBCCR has been presented. According to this proposal, the BCCR would be empowered with the oversight function while the supervisory function would remain in the corresponding supervisory agencies.

2.6.2.2 Deposit Insurance Scheme

At present there is no law or any regulation for deposit insurance. The relevant authorities are currently studying the implementation of a deposit insurance scheme as part of the changes being

⁶² Article 117 of the Law 7558.

⁶³ CAMELS is an acronym for a model created by the federal supervisory authorities of the U.S. to evaluate banks. Each letter represent an evaluation item: C=capital, A=assets, M=management, E = earnings, L=liquidity, S=sensitivity to market risks.

proposed to the LOBCCR. In principle, authorities are considering establishing a protection mechanism for deposits up to ₡2.5 million.⁶⁴

Until these changes are approved, the law only guarantees the deposits kept in State-owned commercial banks, the major players in the system. It is therefore expected that with the implementation of the new deposit insurance mechanism participants will be able to compete in a significantly more leveled playing field.

2.6.2.3 Anti-Money Laundering Measures

On January 10, 2002 Law 8204, the Law on Narcotics, Psychotropic Substances, Non-Authorized Drugs, Capital Legitimate Sources and Connected Activities (*Ley Sobre Estupefacientes, Sustancias Psicotrópicas, Drogas de Uso no Autorizado, Legitimación de Capitales y Actividades Conexas*) was enacted replacing the former Law 7768 of 1998. This law regulates the control, inspection and supervision of the activities related to breathable substances, drugs or remedies and of the products, materials and chemical substances involved in the production of the former. As with the previous law, Law 8204 establishes that it is the State's responsibility to adopt the necessary measures in order to prevent, control, investigate, avoid and hold back all the illegal activities related to the matter of this law.

The financial system Law 8204 prevents and penalizes different activities as a way to avoid the inflow of capital stemming from illegal activities as well as to all the procedures that could be used for legitimizing drug traffic related capital. Article 14 establishes that for the purposes of this law all those institutions being regulated, supervised and controlled by either the SUGEF, SUGEVAL and SUPEN will be considered as financial institutions. Then, Article 15 states that the following activities are also subject to this law:

- Systematic or substantial money exchange operations and transfer through any means such as cheques, bank drafts, bill of exchange and similar ones.
- Systematic or substantial operations of issuance, sale, recovery or transfer of traveler cheques or postal money orders.
- Systematic or substantial funds transfers performed by any means.
- The administration of trusts or the administration of any other resources being executed by persons other than financial intermediaries.

Some of the most relevant obligations and penalties imposed by this law on financial institutions and their supervisors are the following:

- Incoming or outgoing cash transactions either in domestic or foreign currency exceeding USD 10,000 must be registered. These registries must be delivered upon request by the

⁶⁴ Approximately USD 7,300 according to the December 2001 exchange rate.

supervisory agencies and/or by the Joint Anti-Drugs Intelligence Institute (*Instituto de Inteligencia Conjunto Antidrogas*) and will be considered as official proof.

- The owner, director, manager or employee of the supervised financial entities as well as the agent or employee of the supervisory agency will be imprisoned from one to three years if, when exercising their functions, they facilitated the perpetration of money laundering.⁶⁵
- The financial institutions will be responsible for the acts of their employees, managers, directors, owners and other authorized representatives who, acting in that capacity, had participated in the perpetration of any crime specified in this Law. This responsibility will be credited and judged according to the rules previously established in the corresponding law.⁶⁶
- The institutions indicated in Articles 14 and 15 of this Law could be penalized with fines of 0.05 to 0.10 percent of their equity position, according to the severity of the felony.⁶⁷

Finally, the law states that the *Instituto de Inteligencia Conjunto Antidrogas* will have a Financial Analysis Unit⁶⁸ capable of requesting, collecting and analyzing the reports of suspicious transactions produced by financial institutions. The Unit will centralize and analyze such information in order to investigate possible money laundering activities. The information collected by the Unit will be confidential and for exclusive use by the Institute. It can only be revealed to prosecutors, judges or to either national or foreign police organizations with jurisdiction over this matter. Officials who do not adhere to these rules will be subject to penalties prescribed by the Penal Code.⁶⁹

2.6.3 Role of the Securities Regulator

The *Superintendencia General de Valores* (SUGEVAL) was created by the Law 7732 of 1998, the SML, and replaced the former National Securities Commission (*Comisión Nacional de Valores*, CNV), which in turn had been created by the previous SML, Law 7201 of 1990. Prior to the introduction of the CNV only the BNV exercised some sort of supervision, although with a self-regulatory character.

The SUGEVAL is responsible for supervising brokers-dealers, investment funds managing companies, financial groups and financial and non-financial securities issuers. The SUGEVAL is an autonomous entity functioning under the umbrella of the BCCR.⁷⁰

⁶⁵ Article 70 of the Law 8204.

⁶⁶ Article 80 of the Law 8204.

⁶⁷ Article 81 of the Law 8204.

⁶⁸ The previous law also established the functioning of the Financial Analysis Unit (*Unidad de Análisis Financiero*, UAF) with similar powers and responsibilities as those conferred to it by the new law. The previous UAF was part of the Joint Anti-Narcotics Intelligence Centre (*Centro de Inteligencia Conjunto Antidrogas*, CICAD), an autarchy affiliated to the Government.

⁶⁹ Article 106 and 108 of the Law 8204.

⁷⁰ Article 3 of the Law 7732.

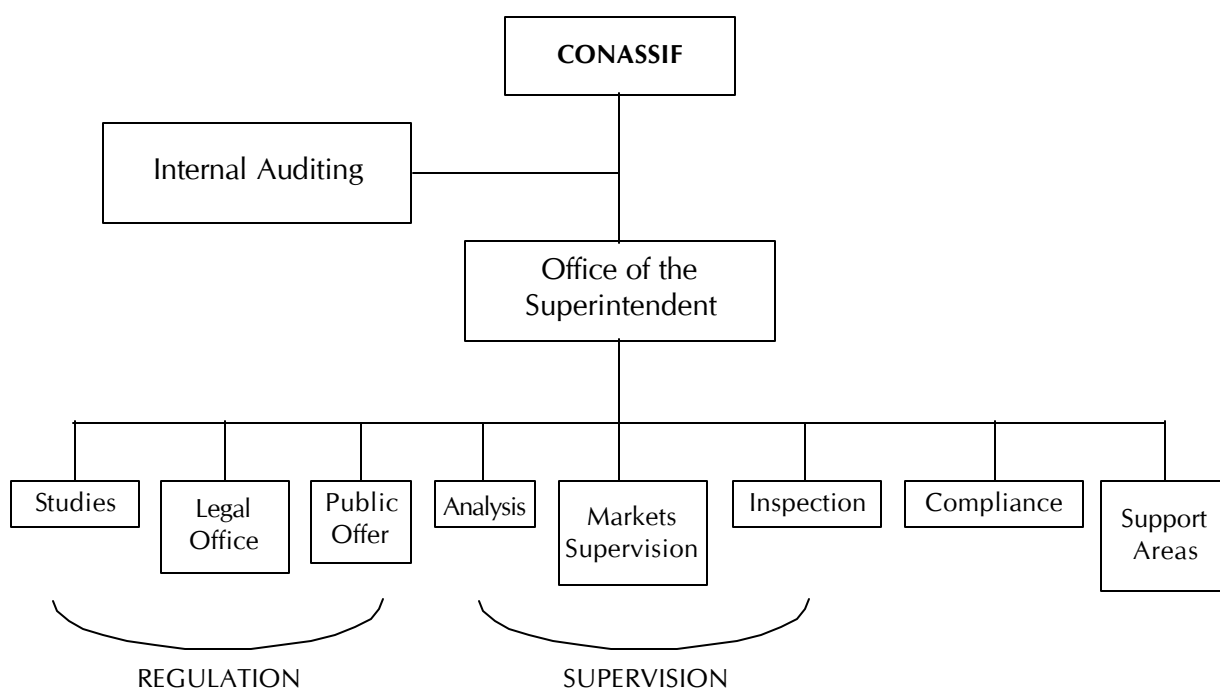
As with the other superintendencies, the SML introduced substantial changes in the organization and powers of this regulatory agency. The functions of the Board of Directors of the former CNV were transferred to the CONASSIF. The Superintendent of the SUGEVAL is entitled to participate in the CONASSIF's meetings although with no voting rights.

The functions of the SUGEVAL are established in Article 3 of the SML. SUGEVAL must watch over the securities markets for transparency, adequate price formation, investor protection and the necessary disclosure of information. SUGEVAL regulates, supervises and controls the securities market, the activities of the individuals or firms participating either directly or indirectly in it and the related actions and contracts determined by law.

Regarding securities clearance and settlement, the SUGEVAL sets and supervises the rules regarding the functioning of CSDs, clearance systems, centralized transaction and information systems for securities transactions. Article 6 of the SML specifically entitles SUGEVAL to regulate the organization and the functioning of the RNVI, including the necessary information and up-dates, to which all individuals and firms participating either directly or indirectly in the securities market (except for investors) must subscribe. All actions and contracts associated with this market as well as all public offerings of securities must also be registered in the RNVI.

The specific functions of SUGEVAL are included in Article 8. These are described in detail in Chapter 8 of this report.

Figure 3: SUGEVAL Organization Chart



Source: SUGEVAL.

2.6.4 Role of the Pensions Regulator

The *Superintendencia de Pensiones* (SUPEN) was created in August 18 of 1995 by Law 7523 as an autonomous entity under the umbrella of the BCCR. The SUPEN regulates and controls private pension systems, which in Costa Rica are called “complementary pensions plans”⁷¹, as well as the medium and long-term capitalization plans. These plans are operated by regular companies called Complementary Pension Plans Managing Firms (*Operadoras de Planes de Pensiones Complementarias*, OPCs).

SUPEN’s main objectives and functions are the following:

- Watch out for the safety of the resources managed by private pension systems.
- Regulate and control the investment of the corresponding funds and watch out for their safety.
- Establish the requirements and conditions that must be complied with by any person or firm wishing to manage private pension plans.
- Authorize the pension plans, determine the rules, and assess the financial soundness of the investment funds.

As with the SUGEF and the SUGEVAL, the SUPEN operates under CONASSIF’s direction.

2.7 THE ROLE OF OTHER PRIVATE AND PUBLIC SECTOR ENTITIES

Besides the BCCR, the supervisory agencies and the financial institutions, there are other institutions participating in the securities and payments clearance and settlement system of Costa Rica, either as direct participants or as supporting institutions. A description of the most important of these institutions follows.

2.7.1 The Ministry of Finance and Public Credit

Three big areas comprise the Ministry of Finance (MH): revenues, financial administration and central administration.

The revenues area is linked to tax collection and it is comprised by the following units: Department of Taxation, Customs National Service, Department of the Finance, Tax Inspection and the Customs Courts.

⁷¹ These pensions complete the basic regimes that are: invalidity, death and old age of the Social Security Institute of Costa Rican, pensions of teachers and of officials of the judicial system, and the pensions that are paid through the national budget.

This area is related to the ILI, the service provided by the SINPE for tax collection and government payments. At the end of 2001 the MH implemented the electronic tax return system using the Internet (SITEL)⁷² for big taxpayers, some of who paid their taxes using the Direct Debit system of the SINPE. In the future it is expected that more taxpayers will pay their taxes by means of electronic transfers.

The Financial Administration area includes the units in charge of controlling the Central Government's goods and services expenses, including: the National Treasury, National Accounting, National Supply, National Budget and the Budgetary Authority. Owing to the connection between MH and the SINPE, all central government payments (payroll, suppliers, cross-border payments and others) are executed electronically, basically through the TEF and the Direct Credits services.

The Central Administration area consists of support areas including: Human Resources Department, Legal Department, Internal Auditing, Financial Department and Internal Supply.

2.7.2 The Bankers' Association

The Costa Rican Bankers' Association (*Asociación Bancaria Costarricense*, ABC) was constituted in December 1983 at the initiative of a group of private banks and financial companies who perceived the necessity of creating an organization to watch over the interests of the national financial sector. Apart from representing the sector, the ABC provides specialized services to the financial system and to other sectors of the economy. It plays an important role in the design of policies for the development and stability of the national banking system.

At present, ABC's members comprise the State-owned commercial banks, the private financial groups and other financial corporations. This means that the ABC is not restricted only to the banking environment but is open also to pensions, securities market, card operators and leasing. Specialized committees have been formed for some of these. Also, there are advisory committees for more general aspects such as human resources, security and internal auditing.

As for the payments system reform effort, the ABC has been contributing through studies and discussion forums. It participates in interbank committees promoted by the BCCR for the development of the SINPE, such as the Advisory Commissions for the Technical Direction of the Payments System, Rules and Procedures for the Payments System, and the Technology and Security of the Payments System.

2.7.3 Private Banks and Financial Institutions Chamber of Costa Rica

The *Cámara de Bancos Privados e Instituciones Financieras de Costa Rica* was founded in 1968 under the original name of Costa Rican National Chamber of Finance (*Cámara Nacional de Finanzas de Costa Rica*). At that time it gathered only non-banking financial entities, as private banks were not allowed to operate in the country. At present its members include private banks as *Banco BCT*, *Banca Promerica*, *Banco de Crédito Centroamericano* and *Banco San José*.

⁷² For further information see the web site www.hacienda.go.cr.

In the past the Chamber played a key role for the creation of the BNV by elaborating the first project that eventually gave birth to it.⁷³ It also participated in the drafting and subsequent reforms of the different banking and financial laws enacted since its creation. Nowadays, it focuses on representing its associates, training and the delivery of information services.

⁷³ Due to legal limitations of the Chamber for being a non-profit association, the stock exchange project was executed by some of its individual associates and by the BCCR.

3 PAYMENT MEDIA USED BY NON-FINANCIAL ENTITIES

3.1 CASH

According to the LOBCCR, the currency in Costa Rica is the colon. Coins and bills issuance is an exclusive right of the BCCR. Neither the State nor any other legal or natural person can issue payment instruments circulating as legal tender. The colon is divided in one hundred cents.

At present the monetary issuance consists of bills varying from five to ten thousand colones and coins from one to five hundred. The coins with low value, one and two colones, are not commonly used. Similarly bills of low values from five to one hundred, are not widely used. In 1998 bills of two thousand and ten thousand denomination were put into circulation.

Cash is generally used for very low value transactions. Cheques and debit and credit cards are used for larger value transactions. As of December 31 2001 total currency in the hands of the public amounted to \$158,090 million, equivalent to 2.9 percent of the GDP.⁷⁴

The only foreign currency frequently circulating in Costa Rica is the U.S. dollar (USD). Although not a general practice, some commercial establishments, especially those related to tourism activities, accept transactions directly in this currency at the daily exchange rate. The Costa Rican reserves in foreign currency are mostly denominated in USD. As of December 31, 2001 the net international reserves were USD 1,330 million.

The BCCR is currently working on a new model for the management of cash. This model has three components: cash market, auxiliary custodies and central bank treasury. The goals associated with these new mechanisms are to reduce the risks associated with cash handling, reduce costs both for the BCCR and the commercial banks and more generally, to improve service to the banks. These projects are described in more detail in Section 4.5 of this report.

3.2 PAYMENT MEANS AND INSTRUMENTS OTHER THAN CASH

Besides cash, cheques, credit and debit cards and smart cards (electronic purse) are generally used as payment means in Costa Rica.

3.2.1 Cheques

According to the Commercial Code, the cheque is "...an unconditional payment order drawn on a bank and payable at sight..."⁷⁵. Thus, chequing or current bank accounts are part of M1, together with the cash in the hands of the public.

⁷⁴ Preliminary data.

⁷⁵ Article 803 of the Commerce Code of Costa Rica. The third chapter of this Code describes the legal underpinning of the cheque as a payment instrument as well as the responsibilities of the holder of a chequing account, among other issues.

The use of the cheque is frequent, although in recent years, and particularly for low value transactions, merchants tend to prefer payments made with debit or credit cards, mainly due to security considerations. For this reason, agreements between the banks and the merchants by which the latter promise to accept cheques as a payment instrument have become common.

In 2001 the cheque clearinghouse processed an average of 43,000 cheques every day, of which 96 percent were denominated in colones and the rest in USD. The average value of cheques in national currency was ₡596,004 while the one for USD denominated cheques was USD 10,655.

To begin implementation of the automated cheque clearing service, the BCCR introduced a series of basic requirements for cheques in order to facilitate their individual and collective processing. These new requirements are related to physical characteristics such as the printing, inks, size, paper, security features and distribution of spaces. With respect to the last characteristic, the target is that cheques provide a space for future data that might be necessary although not essential (e.g., the logo of the account holder), which will not interfere with the necessary and mandatory data spaces (e.g., the magnetic strip, the information about the paying bank, etc.). Moreover, the requirements entail minimum security measures, such as the quality of the materials used to print the cheques, in order to prevent counterfeiting or the improper use of cheques.

The most important change in physical standards is the mandatory inclusion of the magnetic stripe that provides vital information about the document's number, the client's account and the transaction code. This information is mandatory and must be included by banks before delivering cheque books to their clients. The financial institution receiving a cheque has the option to aggregate its amount to the magnetic strip.

The commercial banks still exchange physical cheques and there is no cheque truncation. However, the interbank committees have been discussing this matter and cheque truncation might be implemented during 2003.

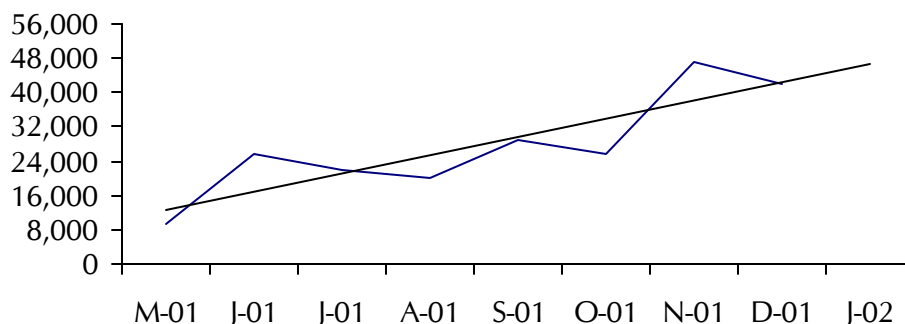
In the same direction and in preparation for cheque truncation, one of the major changes to the Commercial Code regarding cheques consisted of the reduction in the number of endorsements allowed for each cheque. It was determined that cheques written to individuals could be endorsed only once, while for cheques written to firms no endorsement would be allowed. Also, it was established that a microfilm or a digital image of a cheque properly authenticated would have the same legal value as the original physical document.

3.2.2 Direct Credits / Debits

Direct Credits

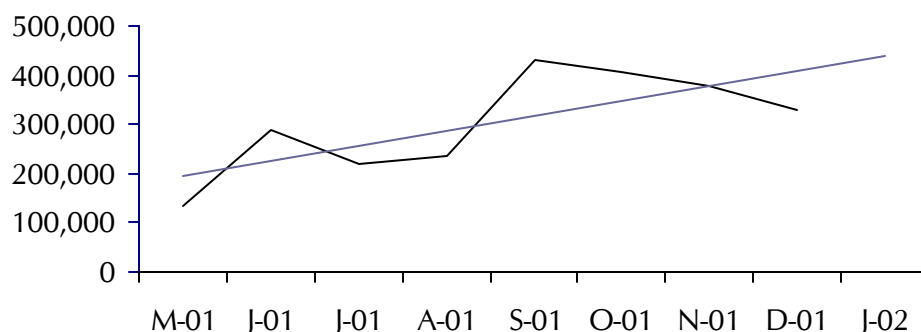
The Direct Credit service started to function in May 2001 to facilitate the payment of payrolls, suppliers, creditors and other services. This service has been very well accepted since its beginning, especially by the Ministry of Finance (MH), which between May and December 2001 generated 86.6 percent of the total volume, followed by the Costa Rican Social Security Institute and the BCCR. Almost all payments made through the Direct Credit service are denominated in domestic currency.

Chart 1: Direct Credit Service: Transacted Value
(monthly flows in millions of colones)



Source: BCCR.

Chart 2: Direct Credit Service: Volume of Transactions
(monthly flows in units)



Source: BCCR.

As may be observed in Charts 1 and 2, the trend is positive for this service both in terms of volume and transacted value. The average value of a single payment during the May – December 2001 period was ₡91,042. In December 2001 about 300,000 transactions were executed, that is, a daily average of 17,300 transactions..

Direct Debits

The Direct Debits service targets the collection of the payments that clients make to public and private institutions on a regular basis. This service has been in operation since December 2001 and the first transactions were carried out by the Ministry of Finance, particularly those related to the collection of taxes from major taxpayers.

3.2.3 Payment Cards

In Costa Rica the use of both credit and debit cards is frequent. The system is open, that is, the banks and other entities can offer different cards of different brands and the relationship with

merchants is not exclusive. Although every issuer has its own brands to identify its products (there are nearly 235 different credit cards), most cards are associated with international brands such as VISA, MasterCard, Diners Club and American Express, and to a lesser extent with local brands such as Agrimax, ST and BCT. Data on the use of cards are presented in the Statistical Appendix in Series A Tables.

3.2.3.1 Credit and Debit Cards

The legal framework for credit cards is provided by the General Law for Public Administration (*Ley General de la Administración Pública*),⁷⁶ the Law for the Promotion of Competition and Consumer Protection (*Ley de Promoción de Competencia y Defensa del Consumidor*), the Law 7472 of December 20, 1995 and its modifications, and the Executive Decree 28712-MEIC "Regulations for Credit Cards" of May 26, 2000.

At present in Costa Rica there are two credit and debit card processing organizations, Credomatic⁷⁷ and ATH⁷⁸, and 24 credit card issuing firms. The latter can be divided into three groups: i) banks; ii) non-banking financial firms; and, iii) non-financial firms.

From the consumer's point of view, the Ministry of the Economy controls these enterprises, particularly with regard to the information regarding interest rates, fees and other charges, terms and additional benefits. On the other hand, from the financial point of view SUGEF has direct control over banks and non-banking financial entities. It also has control over non-financial issuers when they are part of a financial group.

Owing to the fact that the traditional savings accounts using a booklet were transformed into electronic accounts, the use of debit cards increased significantly. Although booklets are still used in some entities (or in specific cases such as foreign currency accounts), currently the accounts of newer clients operate without this document and the registries are electronically posted through the use of a card. Besides giving access to cash in ATMs debit cards are also used to make purchases with affiliated merchants. In the case of current accounts cheque books are still very frequent, although the clients can also have a card with these same functions.

Some banking entities have launched new products combining the use of dual cards (credit – debit) associated with at least one current or savings account with electronic transactions through the Internet and also combining USD and/or colones denominated transactions.

3.2.3.2 Automated Teller Machines (ATMs) and Points of Sale (POS)

At the beginning of year 2001 in Costa Rica there were in operation about 600 ATMs working through five partially interoperable networks. Two of these networks belong to private firms, ATH⁷⁹

⁷⁶ When the issuer is a State-owned bank.

⁷⁷ Credomatic is a private firm affiliated to the *Banco de San José*.

⁷⁸ ATH is a private firm that gathers the private banks with the exception of *Banco de San José*.

⁷⁹ By mid year 2001, ATH had 114 operative ATMs.

and *Red Total*⁸⁰, while the three biggest banks in the country, *Banco Nacional de Costa Rica*, *Banco de Costa Rica* and *Banco Popular*, all State-owned banks, have their own network.

Credomatic and ATH also handle electronic funds transfers at the point of sale (EFTPOS) networks. At the end of year 2000 in Costa Rica there were about 7,500 POS where credit and debit cards and in some cases electronic purses may be used (see Section 3.2.4).

3.2.3.3 Prepaid Cards

Two kinds of prepaid cards circulate in Costa Rica. Both are associated with telephone services. The chip card carries a micro electronic processor that holds a predefined value equivalent to what it is worth. The other card carries a numeric code that needs to be dialed before calling. Of the latter there are two kinds: one for local calls (*Colibrí* 197) and the other for international calls (*Viajera Internacional* 199). These cards are not rechargeable and single purpose. Although payphones working with coins still exist, these cards became the most frequently used payment means for use of the public telephone services.

Although multipurpose cards do not yet exist, according to information published by the Costa Rican Institute for Electricity (*Instituto Costarricense de Electricidad*, ICE) at its web site,⁸¹ there is currently a project to substitute current payphones with intelligent terminals that will allow the use of multiple payment means. Additionally, due to the technological advances, the current chip cards could transform themselves into electronic purses, increasing their usefulness.

3.2.4 Smart Cards - Electronic Purses

Smart cards⁸² appeared for the first time in Costa Rica in the mid nineties and at present two products providing the facility of the electronic purse are circulating.

The two electronic purses operating in Costa Rica are the Mondex⁸³ (international franchise) and *Futura 3000*. The chip of these cards have the capability of storing money as well as other information and can be associated either with a credit or a debit card. Cardholders may use ATMs or other devices, electronic or via telephone, to transfer money balances to the chip.

In both cases, as a strategy to increase the use of the electronic purse, the firms operating these cards have established agreements with universities and merchants so that their cards, besides providing credit and debit services and electronic purse, can be considered as identifications. For example, the traditional identification card of university students was transformed into a smart card allowing the use of the electronic purse facilities through the magnetic bank of a debit or credit card.

⁸⁰ Red Total is a private firm belonging to the Group of *Banco de San José*, who also owns Credomatic. Red Total has 84 ATMs that are not connected to the other networks.

⁸¹ For further details see www.icetel.ice.go.cr/esp/proyectos/protelefonía/html.

⁸² A smart card is a plastic multipurpose card combining different facilities such as debit, credit and electronic purse. It has an embedded microprocessor where financial and non-financial data can be stored and processed.

⁸³ Mondex is a trademark owned by MasterCard.

At the end of 2001 there were about 100,000 smart cards in circulation that could be used in about 2,000 affiliated merchants.

3.2.5 Electronic Funds Transfers

Electronic funds transfers are very common for high value transactions, either among banks or between third parties.

During 2001 the interbank electronic funds transfer service (*Transferencias Interbancarias*, TI) processed about 40,000 transactions. Nearly 78 percent were denominated in local currency and the average amount per transaction was ₡136 million. The average amount of USD denominated transactions was slightly below USD 1 million.

On the other hand, the electronic funds transfer service by/to third parties (*Transferencias a Terceros*, TT) registered an accumulated flow of 31,000 operations in the same period. As in the case of the TI, almost 75 percent of the transactions were denominated in local currency with an average value of ₡65 million. The average value for USD transactions was USD 240,000.

3.3 NON-CASH GOVERNMENT PAYMENTS

All central government payments are handled on a centralized manner and executed through the SINPE. The Direct Credits service is used in the vast majority of cases. Details on government payments and collections are provided in Chapter 4.

4 PAYMENTS: INTERBANK EXCHANGE AND SETTLEMENT CIRCUITS

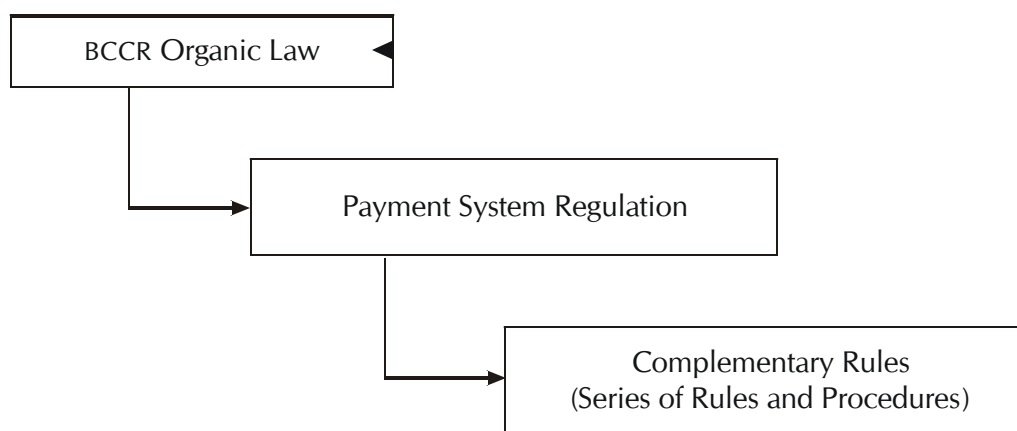
4.1 THE REGULATORY FRAMEWORK FOR CLEARINGHOUSES

The Organic Law of the Central Bank of Costa Rica (LOBCCR) of 1995 empowers the BCCR to organize and regulate the functioning and the operation of the payments system. Also, it grants the BCCR the authority to define the necessary conditions for the system to be efficient, thereby guaranteeing all clients the timely receipt of the value of the payment instruments settled through the system.

On the basis of this legal authority the BCCR elaborated the Regulations for the Payments System (*Reglamento del Sistema de Pagos*). These documents require the approval of the Board of Directors of the BCCR and include all the general aspects regulating the functioning of the different payment instruments processed by the system developed by the BCCR as well as the settlement on the reserve accounts that financial institutions hold at the BCCR. There is also a Set of Complementary Rules and Procedures (*Serie de Normas Complementarias y Procedimientos*) that constitute a compendium of rules for all operational aspects of each payment instrument.

Figure 4 shows the hierarchical levels that integrate the legal framework that regulates the system developed by the BCCR.

Figure 4: Regulatory Framework of the Payment System



Source: BCCR.

In recent years the BCCR developed the *Sistema Interbancario de Negociación y Pagos Electrónicos* (SINPE), a robust and modern technological platform through which it has become the operator and clearance and settlement agent of several payment instruments. Table 7 shows the number and type of participants in the SINPE.

Table 7: Institutions connected to the SINPE
(as of June 2002)

<i>Type of Entity</i>	<i>Number</i>	<i>Totals</i>
Financial Entities , of which		60
Central Bank	1	
Banks Created by Special Laws	2	
State-owned Commercial Bank	3	
Private Commercial Banks	16	
Non-Banking Financial Entities ^(a)	12	
Savings and Loans Mutuals	3	
Savings and Loans Cooperatives	9	
Brokers – Dealers	14	
Others		5
Ministry of Finance		
National Insurance Institute		
Ministry of Planning		
Costa Rican Social Security Institute		
Stock Exchange		
Total		65

Source: BCCR.

^(a) Includes ATH.

The SINPE has been developed with the active participation of all relevant stakeholders. In order to satisfy and carefully organize all the suggestions and obtain the maximum possible feedback of the different sectors represented in the system, the BCCR organized various commissions integrated by representatives of the various sectors. In particular:

Advisory Commission: Responsible for the analysis of the new financial services and functionalities developed in the system. Representatives must reach a consensus within the sector they represent in order to achieve the high level agreements that are necessary for the progress of the system.

Rules and Procedures Commission: Responsible of the definition, revision and updating of the complementary rules of the SINPE services.

Technology and Security Commission: Responsible for the definition of the improvements and the updating required by the technological platform and the security of the SINPE. It is also permanently responsible for the definition, revision and updating of the security policies to be applied to the SINPE.

Advance Commission: This is a monthly plenary meeting held with the representatives of each of the institutions participating in the system to coordinate issues such as improvements of the current services or the new services to be implemented. Everyone obtains information on the changes to be made in their own systems so that they can interoperate adequately with the SINPE.

The BCCR fostered a very wide participation in the whole process, from the conception, development and implementation of each of the different financial services, taking into consideration all observations and suggestions made by the participants. Currently, it communicates all observations, suggestions and documents, either through the previously cited commissions or through more direct means, making sure that each institution receives the different proposals for regulation, complementary rules and the strategic documents.

4.2 LOW AND LARGE VALUE TRANSFER SYSTEMS DEVELOPED IN THE SINPE

The financial services developed in the SINPE in the last five years are:

Support Services

- Customer Account (CC)
- Real Time Access to the Reserve Accounts

Multilateral Net Clearing Services

- Cheques Clearing and Settlement (CLC)
- Clearing and Settlement of Other Documents (COV)
- Direct Credit Clearing Service (CCD)
- Direct Debits Clearing Service (CDD)
- Tax Information and Settlement (ILI)
- Settlement of External Services (LSE)

Real Time Gross Settlement Services

- Interbank Funds Transfers (TI)
- Third Parties Funds Transfers (TT)

4.2.1 Support Services

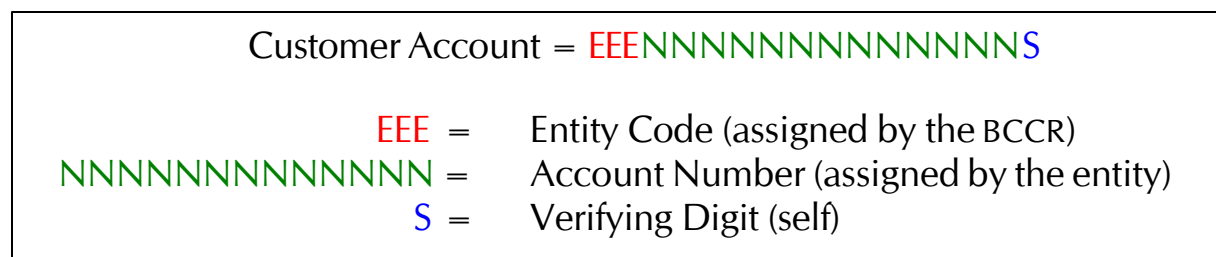
4.2.1.1 Client Account

Before the development of the different financial services, in order to integrate all the financial institutions under a single technological platform the BCCR pushed standardization processes necessary for the

efficient development of the payments system. This standardization was reflected in elements such as: cheque formats, operative processes, electronic registries, templates, etc. Within this process a key was the development and nationwide implementation of a new banking concept, the Customer Account (*Cuenta Cliente*, CC).

The CC consists of an identification number of 17 digits assigned by every financial entity to each one of the chequing and savings accounts of their clients, both in domestic and foreign currency. This number has a standardized structure recognized by the all financial sector institutions. The CC identifies the “financial address” of a client so that the system is capable of automatically channeling all transaction to the corresponding entities. Moreover, being a standardized structure it allows for validations to be performed at the originating institution, thereby guaranteeing better quality of the information inputted in the system.

Figure 5: Customer Account Structure



Source: BCCR.

4.2.1.2 Real Time Access to Reserve Accounts

Through the SINPE, participants have real-time access to their reserve accounts at the BCCR. Participants can obtain on-line information on their balance, account status and historic information about the transactions posted in their accounts. They also have at their disposal facilities to calculate and manage the minimum reserve requirements.

4.2.2 Multilateral Net Clearing Services

4.2.2.1 Cheques Clearing and Settlement (CLC)

The CLC is a service through which the financial entities collect the cheques drawn on other banks that they receive from their clients, either in colones or USD, so that once the cheque is paid the entity may credit the corresponding client.

The CLC works nationwide (i.e. there is only one cheque clearinghouse) and all the cheques received throughout the national territory are electronically presented for payment through the SINPE. Cheques are exchanged physically in a single *ad hoc* facility.

The CLC operates within a cycle of T + 1, which means that the value of a cheque received on day T must be credited to the beneficiary by the following working day. The service cycle is the following:

1. Cheques reception: All cheques received by financial institutions from their clients within the banking hours determined by the BCCR (8.00 a.m. to 5.00 p.m.) must be presented for collection in the same day. For the collection of these cheques financial institutions use a de-centralized process whereby once their offices are closed they electronically process and capture (by means of MICR technology) the information of the received cheques. The file is electronically forwarded to the headquarters. The physical cheques backing up these electronic registries are sent independently.

2. Electronic transmission for collection: Once all the electronic and physical information is collected and consolidated at the headquarters level, an electronic file is sent to the BCCR through the SINPE. This file must comply with the standards determined for the CLC system and must be sent during specific pre-determined hours. The SINPE receives the information from all participants, executes a multilateral clearing process and sends bank a new file to each institution with the details of the cheques that have been presented for collection by all other participants.

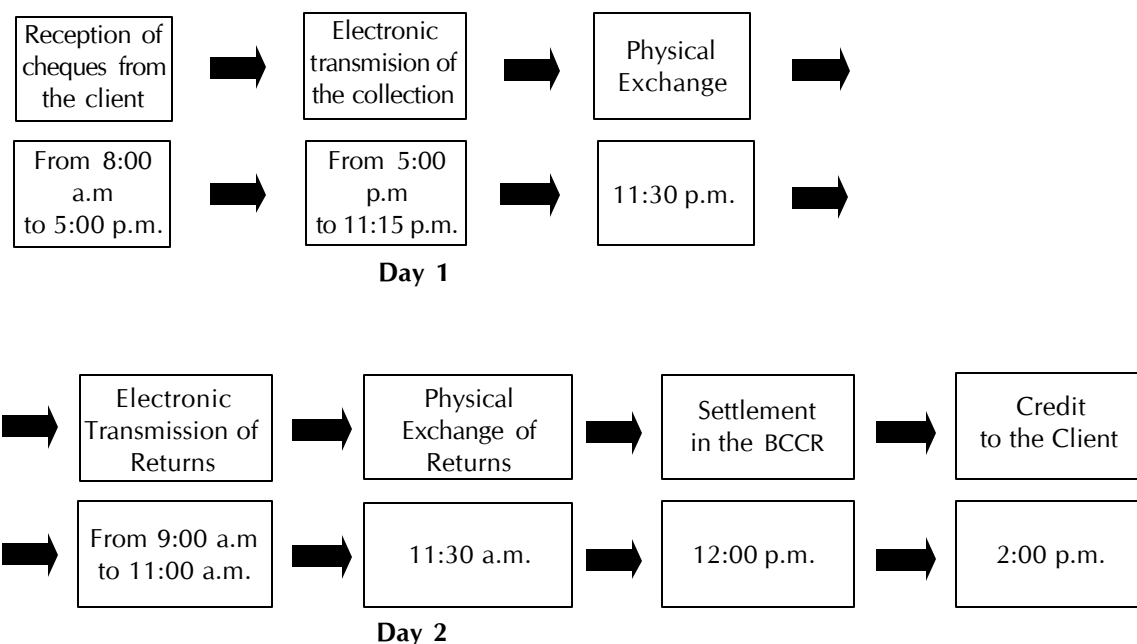
3. Physical exchange: Participants meet to exchange the physical cheques, which must coincide with the electronic file.

4. Electronic transmission of returned items: Once the banks get from the BCCR the file with the cheques they have to pay, since such a file is standardized they can apply it automatically to their current account systems for a first electronic validation of issues such as availability of funds, cancellations, incorrect cheque number, incorrect account number, etc. On the other hand, a physical revision of the cheques is made to verify aspects like endorsements, signatures, color, watermark, paper and others. Once these processes are completed the banks create a returned items file that includes those cheques that did not pass the electronic validation, the physical one or both. The new file is then electronically transmitted to the BCCR through the SINPE.

5. Physical exchange of returned items: The participants organize a new meeting where they physically exchange the returned cheques.

6. Settlement: Once the BCCR receives the electronic file with the returned items it undertakes a multilateral net clearing, obtaining the final position (debit or credit) for each participant. It then transfers this information together with the returned items file. From this moment, participants have up to one hour to solve any liquidity problems they might have before final settlement takes place. Once this hour expires the BCCR executes final settlement on the reserve accounts.

7. Accreditation to the beneficiaries: Once settlement has been executed at the interbank level, banks must credit their clients no later than 2 hours after they received the corresponding funds. Thus, if a client deposits a cheque on day T before 5:00 p.m., it will be credited at the latest by 2:00 p.m. of T + 1 (the next working day). If this were not to be the case, account holders may make a complain to the SUGEF. The SUGEF evaluates the situation and if banks turn to be liable they will be sanctioned. Figure 6 summarizes the clearing cycle.

Figure 6: Cycle of the CLC Service

Source: BCCR.

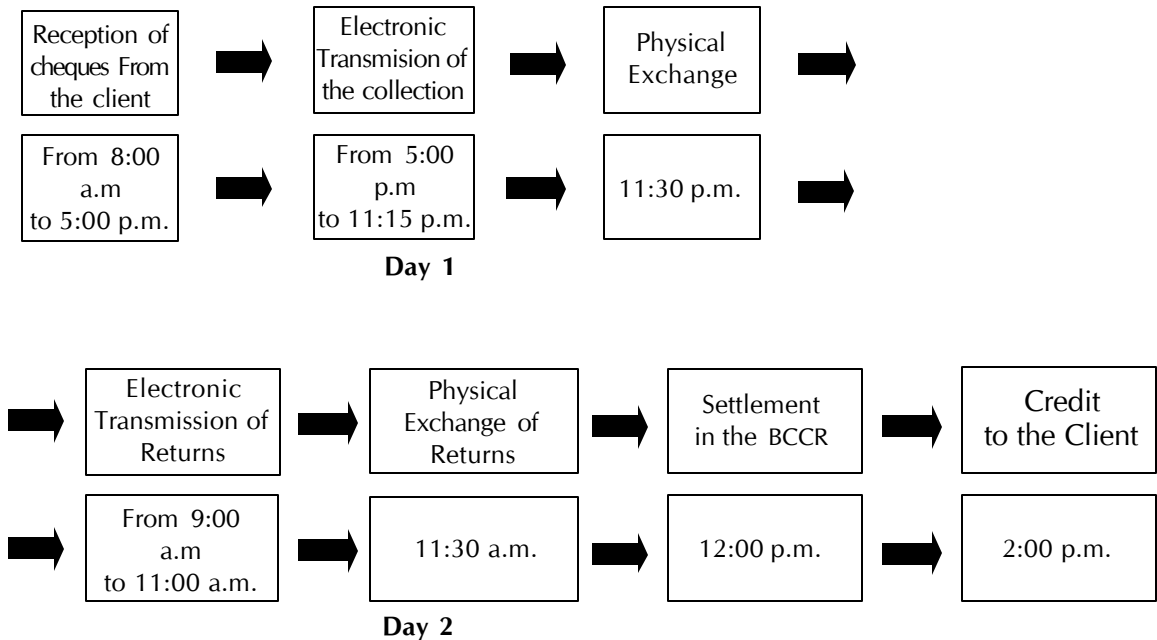
The schedules of the different phases and the electronic standard used for the exchange of files (Extensive Markup Language (XML) Format) are regulated in the complementary rules of the service. This service makes possible the interbank clearance of approximately 50,000 cheques on a daily basis for a total average value of ₡45,000 million (USD 130 million).

4.2.2.2 Clearing and Settlement of Other Documents (COV)

The COV is a service through which the financial entities can exchange other documents received from their clients and issued by other institutions either in colones or in USD, so that once the value of these securities is collected by the receiving entity it may credit the corresponding client.

As with cheques, the COV works nationwide. All documents received throughout the national territory are electronically presented for collection to the BCCR through the SINPE. Physical exchange takes place at an *ad hoc* facility.

The COV works with a T + 1 cycle, meaning that the documents received on day T are to be credited to the corresponding clients during the following working day. The cycle for the COV is identically to that of the CLC. They both use the same schedule for the electronic transmission for collection, returns, physical exchanges and settlement on the reserve accounts at the BCCR. Figure 7 summarizes the clearing cycle.

Figure 7: Cycle of the COV Service

Source: BCCR.

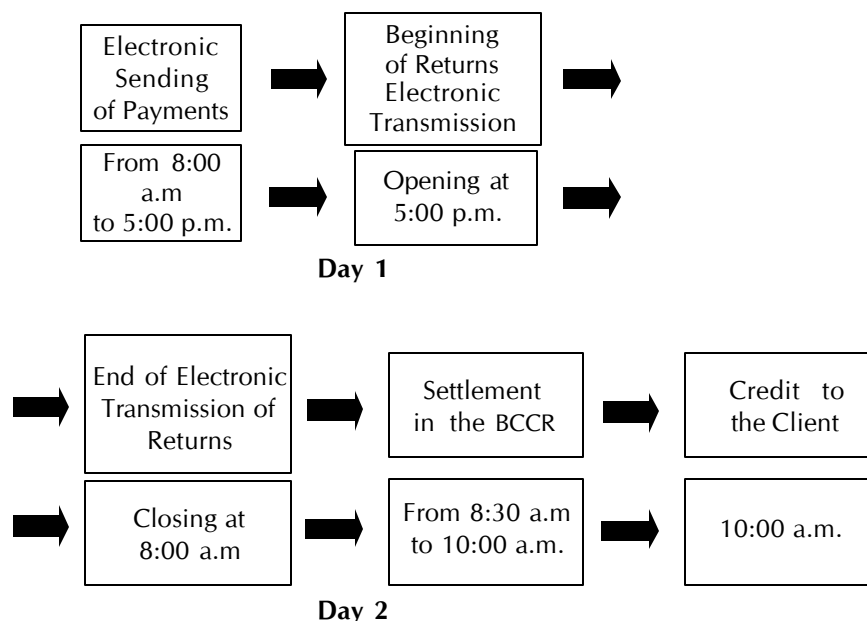
4.2.2.3 Direct Credits Clearing Service (CD)

The CD is a service created for massive payments such as payrolls, suppliers, etc.

It operates under the STP concept (straight through processing). The information required for the clearance and settlement of payment orders is introduced only once into the system through front-end negotiation systems. This makes the CD service rapid and reliable. Moreover, the receiving entity cannot be held liable for any payment execution errors as it is the originating entity that enters the necessary information to execute the operation. This avoids ambiguities and dispersion of responsibilities, thereby increasing the protection to the beneficiaries.

The service works with a T+1 cycle starting from the moment in which the originating client requests the payment service to its financial entity and the transaction is inputted into the system. The cycle phases are the following:

1. **Payment Electronic Transmission:** the originator (the client that pays) orders its financial entity (originating entity) to make a payment. The originating entity sends to the SINPE an electronic file in XML format, which consolidates all the credits requested by its clients during banking hours. The SINPE receives the electronic archives of all the participants, undertakes a multilateral net clearing and sends back a file to the receiving entities with the registry of the payments the rest of the participants are executing. The file details the CC of the beneficiaries.

Figure 8: Cycle of the CCD Service

Source: BCCR.

2. Electronic Transmission of Returned Items: Once they receive the file from the BCCR, the receiving institutions apply it automatically to their current accounts systems in order to validate the existence of the CC detailed in the electronic file. Afterwards, they send back to the BCCR a new electronic file with the corresponding returned items, if any.

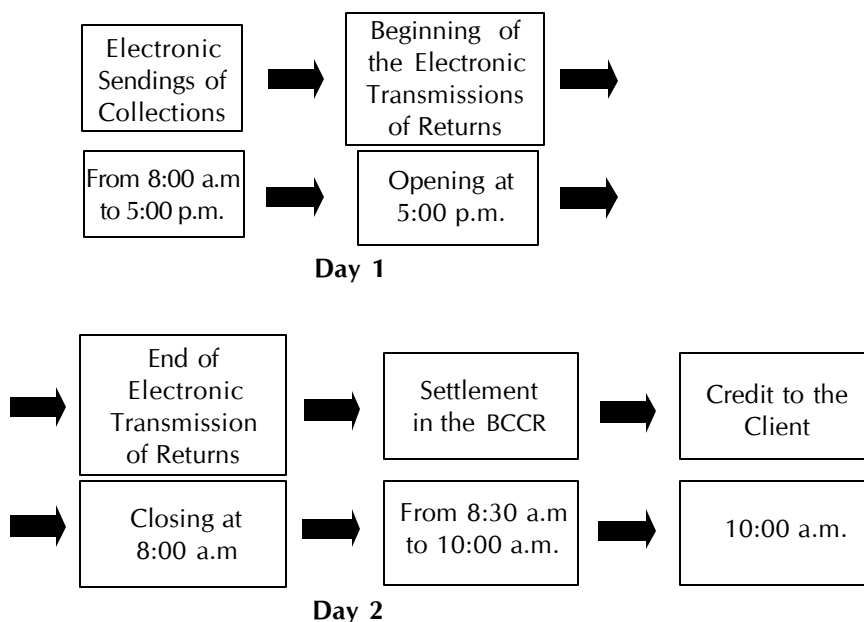
3. Settlement: The BCCR receives through the SINPE the returned items files of all participants, undertakes a multilateral net clearing and executes final settlement on the reserve accounts. Moreover, the BCCR informs the paying entities about the returned items that were presented so that the latter can communicate the situation to their clients.

4. Accreditation to the beneficiaries: once the receiving institutions receive the corresponding funds in their reserve account they must credit their clients and inform them of the transaction. Figure 8 summarizes the clearing cycle.

There are no limits in the CD service in terms of minimum or maximum amounts. However, so far the service has been used mainly for retail payments.

4.2.2.4 Direct Debits Clearing Service (DD)

The Direct Debits service was created for the automatic payment by customers of services such as electricity, water, telephone, magazine subscriptions, schooling, insurance policy, rents and in general any other periodical collection.

Figure 9: Cycle of the CDD Service

Source: BCCR.

As with the CD service, the DD operates under the STP concept. However, for a transaction to be executed through the DD service the issuance of a “Debit Order” (*Orden de Domiciliación*) by the current account holder by which it authorizes the relevant company to withdraw funds from its account is required.

The DD service operates with a T + 1 cycle. The procedure is identical to that of the CD service. They both use the same schedule for the electronic transmission of information, returns and settlement on the reserve accounts at the BCCR. Figure 9 summarizes the clearing cycle.

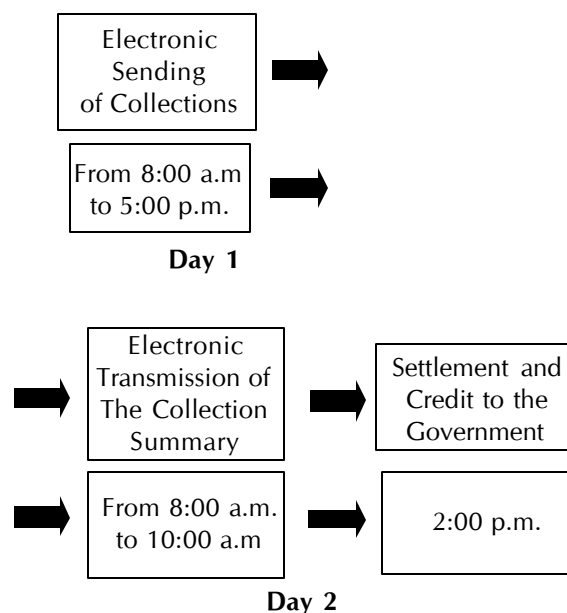
4.2.2.5 Tax Information and Settlement (ILI)

The ILI service was developed to electronically collect the tax payments received by the financial entities on behalf of the Central Government of the Republic.

The Ministry of Finance authorized financial entities to collect taxes on its behalf. These funds are then transferred by the financial entities through the SINPE to the account of the Central Government at the BCCR within a T + 1 cycle. Financial institutions must also transmit electronically the details of these taxes. The latter information is used by the National Treasury and the National Accountancy, both of which have access to the SINPE, for control purposes.

The cycle of the ILI service is the following:

1. Tax Collection: the financial entities collect tax payments made at their headquarters, agencies or branches. They also receive the accompanying documentation. All this information is consolidated at the headquarters of each collecting entity.

Figure 10: Cycle of the ILI Service

Source: BCCR.

2. Electronic Transmission of the Tax Collection Summary: The collecting entities send to the BCCR an electronic file with the summary of the information of the collection divided by tax type, so that it can be processed by the SINPE.

3. Settlement: After the electronic transmission the settlement process is executed. The gross amount is debited from the reserve account of each collecting entity and the account of the Ministry of Finance – National Treasury is then credited. Figure 10 summarizes the clearing cycle.

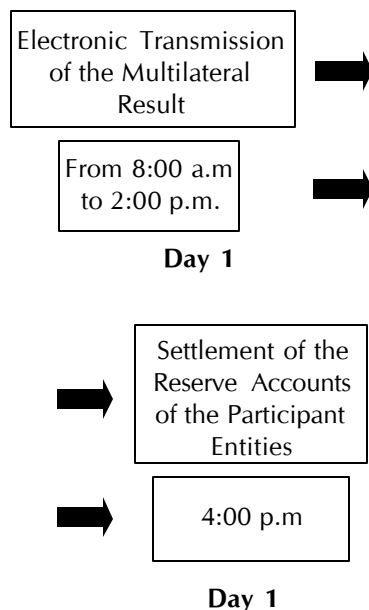
4.2.2.6 Settlement of External Services (LSE)

LSE is a service for the settlement in central bank money (the reserve accounts) of positions stemming from a clearance procedure different from those offered by the SINPE.

At present, this service is used for the settlement of positions arising from the participation of the financial entities in ATM networks and in the stock exchange. However, the LSE service was conceived in a way that in the future it may be used by other markets such as, for example, credit and/or debit cards, electronic purses, and in general any bilateral or multilateral payment processes in which two or more financial entities participate.

The LSE service works within a T cycle according to the following:

1. Electronic Transmission of the Net Bilateral Result: the clearing agent sends to the BCCR an electronic file with the information of the bilateral net positions.

Figure 11: Cycle of the LSE Service

Source: BCCR.

2. Settlement: The BCCR then calculates the net multilateral positions and proceeds with the settlement. For the latter, the BCCR first debits the accounts of those entities with a net debit position and then it credits the accounts of the institutions with net credit positions. Figure 11 summarizes the clearing cycle.

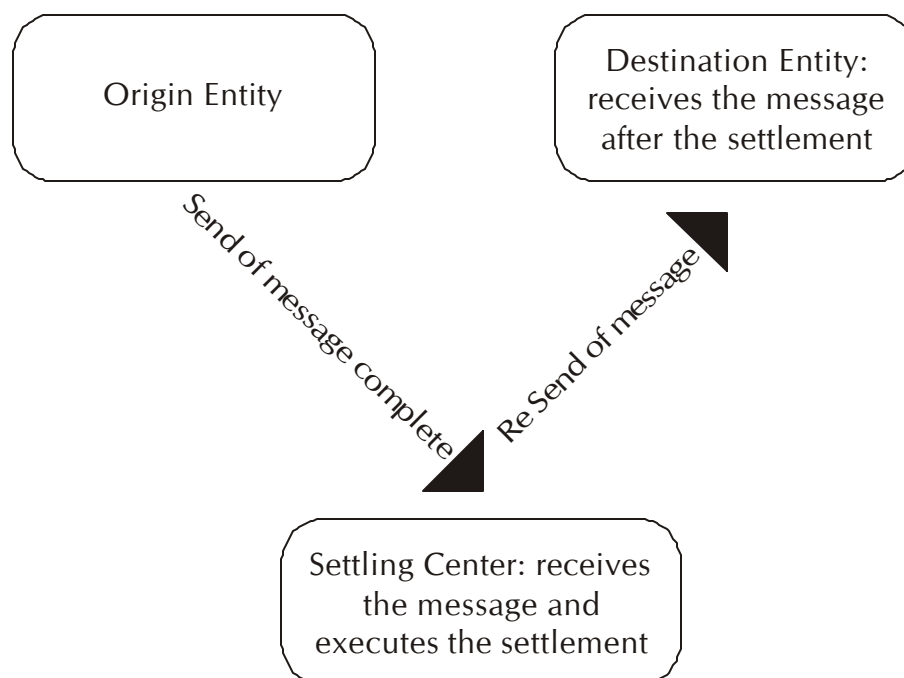
4.2.3 Real Time Gross Settlement Services

The BCCR developed two real time gross settlement (RTGS) facilities within the SINPE. Such facilities now handle a great amount of transactions that previously were settled through the cheque clearinghouse. These facilities have significantly reduced financial risks since highly risky debit transactions (cheques, credit risk, security, operational costs and others) are being transformed into fully electronic credit transactions in which settlement occurs if, and only if, funds are available at the time the transaction is made.

The RTGS facilities are basically configured under the “V scheme” of the BIS. However, due to some specific modifications they actually have what has been called a “W” shape.⁸⁴

The configuration under the “V scheme” involves three steps: sending the message, settlement and the reception of the message.

⁸⁴ For further details see “Real-Time Gross Settlement Systems”, Committee on Payment and Settlement Systems of the Group of Ten Countries, Bank for International Settlements, 1997.

Figure 12: Messages Flow: the “V” Scheme

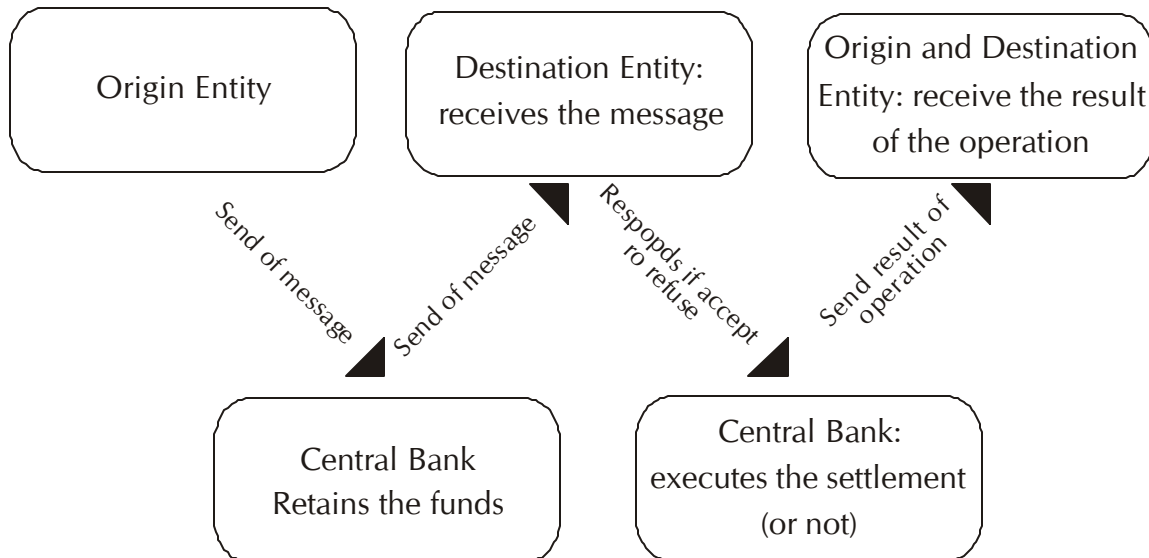
The modification embedded in the RTGS facilities of the SINPE is the possibility for the destination entity to repudiate the transfer, anticipating the following situations: incorrect amount, insufficient or wrong details, wrong currency, cancellation by the originator or message sent out of the established time schedule. In the particular case of transfers among third parties additional causes for repudiation could be that the requested client account was closed or suspended, the amount, currency and/or payment information are incorrect, the account holder rejects the transfer or its account is not activated to receive this kind of transfers.

Allowing the destination entity to repudiate the funds transfer is also in line with the requirements that have been imposed to financial entities in association with anti-money laundering considerations. Thus, if the receiving entity is not sure about the origin of the funds being transferred it may repudiate the transaction.

There is no limit on the amounts that can be transferred through the RTGS facilities. However, due to pricing considerations the amounts are usually large.

4.2.3.1 Interbank Funds Transfers (TI)

The TI service allows a participating financial entity to issue an instruction to transfer funds from its reserve account to that of another participant. The service also allows funds transfer from/to the BCCR, who acts also as a participant and not only as service provider.

Figure 13: Messages flow: the “W” scheme

The IT service operates within a one-hour cycle, since one hour time is the maximum time that is given to destination entities to accept or repudiate transfers. However, since the system allows the automatic acceptance by the destination entity it is in fact considered a real-time or on-line funds transfer system.

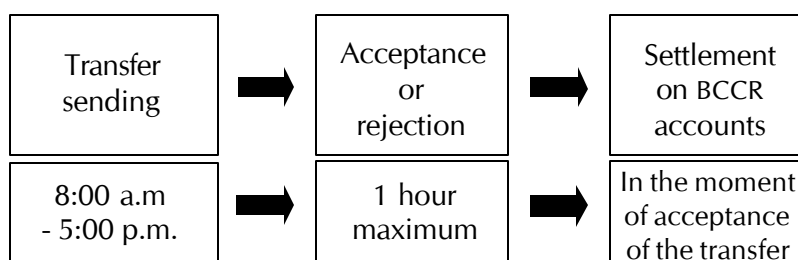
1. Transmittal of Messages: the origin entity issues through the SINPE a payment instruction with the corresponding information to transfer funds from its reserve account to another reserve account at the BCCR. The SINPE withholds the amount of the transfer from the originating entity.

2. Transfer Acceptance or Repudiation: the destination entity has a maximum of one hour, starting from the moment in which it receives the electronic communication, to inform the BCCR, using the same media, that it accepts or repudiates the transfer.

3. Settlement: the SINPE executes the settlement crediting the reserve account of the destination entity once it has received its acceptance. If after the stipulated time the transfer has not been neither accepted nor repudiated by the destination entity, this is interpreted as a signal of acceptance and settlement proceeds. Figure 4 summarized the settlement cycle.

4.2.3.2 Third Parties Funds Transfers (TT)

Through the TT service bank customers may instruct a participating financial entity (originating entity) to send funds to a destination entity and have them credited in a particular Client Account (CC).

Figure 14: Cycle of the TI Service

Source: BCCR.

The TT service works in the same manner as the TI service. The only difference is that the funds are destined to a particular CC in the destination entity, that is, the funds are directed to a third party. The operation cycle is similar to that of the TI service with an additional step represented by the crediting of the beneficiary. Figure 15 summarizes the settlement cycle.

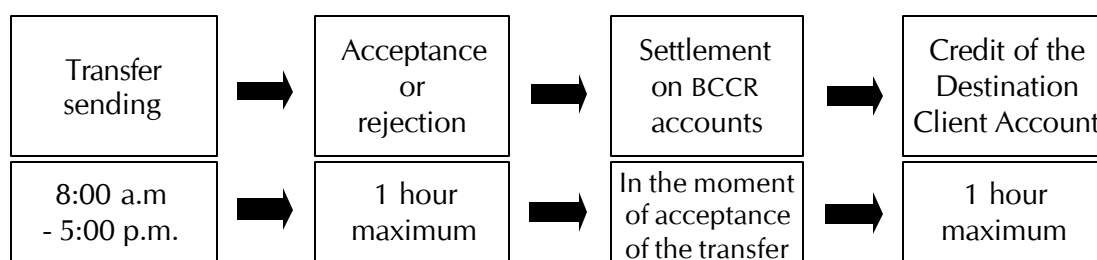
4.2.4 Risk Management

4.2.4.1 Liquidity and Systemic Risks

Risks in the multilateral net clearing services

The BCCR has established risk control measures for the liquidity and systemic risks embedded in the multilateral net clearing services (CL, COV, CCD, CDD and LSE) it provides. The mechanism consists of pools of collateral and follows the “defaulter pays” principle. The main features of this mechanism are the following:

- Amount: rounded moving average for the last 60 days of the net debit positions of each participant in the multilateral net clearing services.⁸⁵

Figure 15: Cycle of the TT Service

Source: BCCR.

⁸⁵ In this calculation extreme positions are eliminated.

- Collateral: debt securities issued by the BCCR itself or by the MH, considered at their current market value.
- Custody of the pledged securities: the securities are deposited in the central securities depository and a lien in favor of the BCCR is established. The securities may be withdrawn only with the authorization of the BCCR.
- Updating of the amount to be collateralized: the amount of the needed collateral is calculated on a weekly basis and communicated to the participants through the SINPE so that they can do the necessary adjustments and comply with it. There is also a daily appraisal of the market value of pledged securities. If necessary, participants are required to make the corresponding adjustments.

In case any financial institution lacks sufficient liquidity during the settlement process of any of the multilateral net clearing services, the BCCR automatically makes a repo transaction with the available collateral under the following conditions:

- Credit amount: up to 80 percent of the market value of the securities pledged by the participant.
- Terms: 1 day extendable to 7 if requested by the participant.
- Cost: the rate previously defined by the Board of Directors of the BCCR.

Risks in the RTGS services

The institution that sends a payment order through any of the RTGS facilities must be assured that it has the necessary funds as the system neither allows overdrafts in the reserve accounts nor has any queuing mechanism. Also, due to the monetary policy regulations management of intraday liquidity is not flexible.

If a payment order is rejected due to insufficient funds the message does not go into a standby status or to a queue while the entity gathers the funds. The option available for participants is to obtain an overnight repo with the BCCR through the MIB system or in the general market through the Liquidity Market (*Mercado de Liquidez*). Once the reserve account of the originating entity has the necessary funds, it is necessary to re-enter the message.

4.2.4.2 Operational Risk

In order to reduce operational risk the BCCR has established several measures, among which the definition of compulsory technological requirements both for the BCCR and the other participants.

Regarding the telecommunications network, the BCCR established that every participant must have two dedicated lines and one shared line for the transmission and reception of files to/from the

BCCR. Also, participants must keep their telecommunications equipment (modems, routers and others) in a safe and adequate site that complies with the defined standards. Additionally, participants must have a minimum of two working stations compliant with the technological standards defined by the BCCR. Every user of a service must have access to both working stations.

The BCCR has a contingency site with equipment and technological characteristics identical to those of the main site. Also, contingency plans were established for each of the technological elements embodied in the system's processes such as electric power, telecommunications, hardware, software and others.

In case a participant faces a situation in which it is not able to transmit its files to the BCCR, it has the option to use the Alternate Operations Hall (*Sala Alternativa de Operaciones, SAO*), which is located inside the BCCR. In order for participants to use this alternative site, they must strictly follow the established procedures, which include all necessary security steps and schedules.

Moreover, the electronic files follow a strict validation process in order to guarantee the quality of the information that navigates through the system. Once the electronic files are created they must pass structure and content validations before they can be transmitted through the system. Some of the contents that are validated are the CC, cycle date, the session (collection or return), batch number and others. Once the SINPE receives the files some of the key data are validated once again.

If an institution is having problems to complete some of the clearance cycle phases within the established schedule, it may communicate this situation to the system operator through the Extranet or other established mechanism. Depending on the severity of the contingency, by means of an Extranet bulletin the operator will inform the rest of the participants of the situation as well as the measures to be adopted to solve it. These measures may include an extension of the closing hour of one phase of the cycle (collection or return) or that returned items be transferred to the next cycle for a specific entity. In the extreme case in which a participant is unable to settle despite his collateral position, an unwinding procedure takes place.

4.3 OTHER SUPPORT SERVICES OF THE SINPE

The BCCR implemented a set of additional functionalities in order for financial entities to efficiently manage the funds they hold at the reserve accounts as well to perform the necessary risk controls and obtain updated information from the SINPE. These functionalities are the following:

- Management of Security Schemes (AES).
- Extranet.
- Agent.
- On-line Analytical Processing (OLAP).

- Call Center.
- Certification of SINPE Users.

4.3.1 Management of Security Schemes

In a system like the SINPE, which manages the funds of financial entities with a daily settlement throughput of approximately USD 300 million, security is a vital element. In this regard the BCCR developed a service called "Management of Security Schemes" (*Administración de Esquemas de Seguridad, AES*) through which the security of the system is managed and access is controlled.

The AES has been developed in order for security to be managed in a de-centralized way, meaning that the participants themselves are those who actually manage and control the security of the system. Participating financial entities must authorize and inform the BCCR of two Persons Responsible for Total Security (*Responsables de Seguridad Total, RST*). These persons are the ones within their corresponding institutions to authorize the users of the SINPE services, or they may designate Persons Responsible for Partial Security (*Responsables de Seguridad Parcial, RSP*), who will help with security management.

The AES makes available to participants all the necessary facilities to exercise a strict control over the users as well as over the transactions the latter execute through the system. There are also exclusive profiles for persons to perform audit actions.

4.3.2 Extranet

The SINPE provides the participants with a very important and functional tool that is the Extranet. It provides on-line access to information about the system, such as the Regulations for the Payments System and the Complementary Rules and Procedures of the SINPE. Additionally, through the Extranet the users may request support and reports on any irregularities that occurred in the use of the services. They may also submit their observations or proposals for system improvements. All these requests, reports or suggestions are handled through a Call Center.

4.3.3 Agent

Because of the permanent relationship with the users of the SINPE, it is necessary to have an expeditious communication tool. Thus, a SINPE "Agent" was created as a part of the system. The agent consists of an "electronic messenger" that alerts and informs the users on any general or specific event that may arise. It also communicates matters of interest for every entity, new software versions, meeting calls for the SINPE commissions, the outcome of particular settlement processes, training events and others.

The agent has been designed in such a way that it allows communication not only with the working station connected to the SINPE but also to any other communication device such as the specific

electronic mail directory, telephone, cellular phone or beeper. The goal is to achieve the maximum possible efficiency and to keep SINPE users perfectly informed on any relevant event of their corresponding institutions in the system.

4.3.4 On-line Analytical Processing (OLAP)

The SINPE has at its disposal huge amounts of valuable and important information, both at an aggregate and detailed level, of all the operations executed through the system. With the idea of making this information useful for the participants, the SINPE developed a facility known as OLAP that allows the participants to obtain this information in a structured form through the use of "data cubes". These statistical data cubes are dynamic and are produced by the system itself according to the user's requirements.

4.3.5 Call Center

Since the beginning of 2002 a personalized care center for the users of the system was implemented in the SINPE. It is based on the very well known concept of a "Call Center", using for this purpose the SIEBEL tool. The Call Center offers customer support, maintenance and general attention to the users in a more efficient way. All user calls requesting help to the SINPE are registered in the Call Center facility as "cases". These cases are then assigned to a particular technician.

4.3.6 Certification of SINPE Users

With the implementation of new services, the SINPE has been growing and as of current date it has approximately 2000 users distributed among the 65 financial entities connected to the system. This has led to the need for the certification of the users in order to guarantee the proper use of the system. Certification is provided by officials of the SINPE Operations Center, the department in charge of system support and maintenance.

However, due to the increasing number of users the first steps are being taken to offer a certified training program. By means of this program the financial entities connected to the system will have the possibility of certifying their officials in the use of the SINPE in order to guarantee the adequate operation of their institution within the system.

4.4 CROSS-BORDER PAYMENT SETTLEMENT SYSTEMS

Until the second semester of 2001 the financial institutions had two options to transfer funds to/from abroad: connecting to SWIFT or making transactions through the BCCR.

In the first scenario, at the beginning of 2001 about 10 banking institutions were connected to SWIFT. For the rest of the financial institutions the system worked as follows. They would send a Telex to the BCCR requesting funds transfers. Then the BCCR would make the requested transactions using independent equipment and systems provided by two correspondent banks.

By the end of 2001 this mechanism changed when the BCCR itself connected to SWIFT. With this service the BCCR has access to a direct multilateral connection, enlarging the spectrum of financial institutions around the world with which it can execute financial transactions in a secure and agile way.

The connection to the SWIFT by the BCCR helps the country's financial system as a whole and particularly those institutions that due to cost considerations cannot afford a connection of their own. Financial entities now send to the BCCR their request for funds transfer through the Interbank Funds Transfer (TI) system.

4.5 MAJOR PROJECTS AND POLICIES BEING IMPLEMENTED

4.5.1 General Aspects

Legal

The LOBCCR gave the BCCR the power to organize and regulate the payments system of the country. This legal framework has allowed the creation of Regulations for the Payments System and the complementary rules regulating the different services presently in operation. However, the progress reached has shown the need for a revision, evaluation and modification of some other related laws such as the Commercial Code, the LOSBN and others, or even to evaluate the possibility of creating a Payments System Law that integrates all the legal elements associated to this important system.

Technological

The SINPE was developed using state of the art technology, which makes it a secure and agile system. However, there is still the challenge of keeping it updated in order to avoid a rapid obsolescence. On the other hand, because of the volume of financial transactions passing through the system, it is necessary to ensure that the continuity of the service is always maintained. Thus, important resources and efforts must be allocated in order to consolidate a solid contingent platform that guarantees the normal functioning of the system.

Administrative and functional structure

During its first 5 years the SINPE project was controlled by the General Management of the BCCR. It had no clear place within the administrative structure of the central bank. Starting from 2001 the payments system activity was integrated into the formal structure of the BCCR as part of the Financial Services Division, responding directly to the General Management. The latter has given dynamism to the Division, transforming it into a modern one in accordance with the automation environment created with the development of the SINPE.

In 2001 other changes were made to cope with the various tasks that a modern payments system involves. Three specialized areas have been created to address regulatory issues, system operation and payments system oversight.

Payments system oversight

Recently, the Payments System Oversight Department was created within the BCCR. This administrative structure will be responsible for ensuring the fluidity, stability and efficiency of payment systems. This area is charged with identifying and handling the relevant risks as well as of ensuring compliance with regulations and rules.

4.5.2 New Services

Cheques Clearance and Settlement

New regulations for cheque truncation are being included. The current proposal has already been endorsed by the Commission of Rules and Procedures of the payments system and it is expected to become operational by the beginning of 2003.

Currency Management (Bills and Coins)

Proposals in this regard may be classified in two projects: the Cash Market and the Auxiliary Custodies:

- Cash Market: This service will enable financial entities to buy and sell domestic currency surpluses among themselves. Financial institutions will communicate electronically through the SINPE technological platform. This program is expected to expedite the currency offer and demand process, thereby lowering the operational costs associated with the transportation of bills and coins since movements to and from the BCCR will be reduced. This service is expected to become operational by the end of 2003.
- Auxiliary Custodies: At present the physical movement of the currency from the financial entities to the BCCR vaults is mandated. With the Auxiliary Custodies service the custody would be de-centralized. Financial entities will be allowed to keep a percentage of the legal reserve requirement in their own vaults. Moreover, financial institutions would be allowed to make deposits and withdrawals electronically, thereby reducing cash handling and the transportation costs. This service is expected to become operational by the beginning of 2003.

Public Debt Deposits

Through the SINPE platform financial entities will be able to make investments in the BCCR. The service will be fully integrated and several categories such as overnight, short term, electronic window and auction will be included. This service is expected to become operational by the end of 2003.

SINPE-SWIFT interface

An interface between the SINPE and SWIFT is being developed with the idea of extending SWIFT services to all financial entities connected to the SINPE, thereby making use of the economies of

scale. It is expected that the SINPE-SWIFT interface will be ready by the end of 2002/beginning of 2003.

SINPE Assistance

As the SINPE has been developing a series of support services within the system, it is important that these facilities be readily accessible to users in a friendlier environment. Thus, a tool called “assistance bar” is being developed. This will allow the user to access facilities such as the legal framework, communications, the OLAP tool, service evaluations and others.

ISO Certification

A quality management review of the system using the ISO 9001 approach was started in 2002. This process involves the definition of quality processes and manuals, elaboration of quality procedures and quality registries, and establishing an efficient management system for all these documents (through the Microsoft Share Point Portal Server tool). The ultimate goal is not the ISO certification itself but rather to establish a process by which the system may be continuously improved.

The quality management process will use as one of its quality parameters the fulfillment of the CPSS Core Principles for Systemically Important Payment Systems.

SINPE Services Evaluation

Related to the Quality Management process, an evaluation process has started in which system users have the opportunity to evaluate the quality of the services being offered through the SINPE. The aspects or the variables subject to evaluation will be determined by the entities as well as the valuation mechanisms. The results will be presented to the BCCR Management. The process will also involve an assessment of the financial institutions, which aims at evaluating the level of participation of the entity and its representatives in the development of the system, their contributions for the improvement of the system and how well they have been adapting to new trends.

5 SECURITIES, MARKET STRUCTURE AND TRADING

INSTRUMENTS

5.1 FORMS OF SECURITIES

According to Article 2 of the Securities Market Law (SML), securities are either economic or patrimonial rights, embodied or not in a document, that can be legally negotiated in financial markets.

Securities are mainly represented by means of physical certificates and a portion is immobilized in the central securities depository, *Central de Valores de la Bolsa Nacional de Valores, S.A. (CEVAL)*. Brokers-dealers, banks and pension funds participate directly in CEVAL.⁸⁶ In May 2001, 68 percent of the fixed rate securities and 53 percent of stocks were immobilized. Similarly, 98 percent of the international debt securities and 100 percent of the international stocks were also immobilized.

Regarding the issuance of dematerialized securities, the SML establishes that those securities registered in the National Registry of Securities and Intermediaries (RNVI) may be issued either in book entry form or physically, the selected method being applicable to all the securities comprising the same issuance.⁸⁷ Representation by means of book entries is irreversible and SUGEVAL may establish in general or for certain categories of securities that representation by means of book entries be a necessary condition in order to get a public offer authorization. Securities represented by book entries are constituted once they are registered in the corresponding books.

At the time this report was prepared no dematerialized securities had been issued. The Government still issues debt in a physical form and approximately 40 percent of the Government's outstanding debt was not yet immobilized.

5.2 TYPES OF SECURITIES

Within the legal definition, the following are considered securities:⁸⁸

- Equities issued by companies as well as any other security that may entail equity-subscription rights.
- Obligations and similar securities representing a loan or a syndicated loan to the issuer.

⁸⁶ The banks and the pension funds only have non-operational custody accounts and the securities in these accounts can only be negotiated when transferred to a broker-dealer's account or to a MIB account in the case of the interbank money market.

⁸⁷ Article 115 of the SML. Additionally, transitory Article VII of the SML states that after a year of the enactment of this Law the CONASSIF may establish mandatory book entry securities transfers, including all securities publicly offered.

⁸⁸ Article 3 of the Regulations for the Public Offering of Securities.

- Documents such as promissory notes and bill of exchange having the nature of securities, according to the law or commercial practices.
- Certificates issued by close-end investment funds.
- Securities in book entry form, conforming to requirements determined by the SML and the correspondent regulations.

Securities suitable to be traded in a stock exchange

Only those securities issued in accordance with the rules contained in Section III of the Regulations for the Public Offering of Securities (*Reglamento de Oferta Pública de Valores*, ROPV) are considered suitable for trading in a stock exchange. According to Article 10 of the SML, exception is made for the individual securities issued by those entities supervised by the SUGEF.

Securities to be traded in stock exchanges cannot be the object of a public offering if limitations and restrictions were previously decided in reference to their transferal regime in a way that impersonal transfers may be impeded or made difficult. If these limitations were decided after the public offering was authorized and if the securities are shares representing at least 50 percent of the firm's equity in circulation, the shareholders who decided these limitations would have to make a public offer for the exclusion of the rest of the capital.

5.2.1 Shares and Other Securities Representing Equities

The stock market in Costa Rica is relatively small. Total traded value in the secondary market by June 2001 reached ₡13,810 million, 95 percent higher than the traded value for the first six months of 2000. Despite this growth, the securities market is basically a public debt market. Equities transactions represented merely 0.3 percent of the total traded value in the BNV in the first semester of year 2001.

Shares

In Article 120 of the Commercial Code a share is defined as a security representing and transferring a partnership status. Common shares grant identical rights, represent equal portions of the firm's equity and must be issued as registered securities. Both common and preferred shares and other similar instruments may be issued either in domestic or foreign currency.

Subscription Rights

Article 46 of the SML establishes preferential subscription rights for shares. These rights belong to the buyer (shareholder). If the buyer wants to exercise this right within the time framework established by stock exchange regulations for that purpose, the seller (issuer) has to provide him with all the facilities to exercise this right. Alternatively, the seller may exercise this right on behalf of the shareholder, provided that the latter has given the necessary funds.

Trust Certificates Issued by Investment Funds:

Participations or property right of investors in any investment fund are represented by share certificates (*certificados de participación*). Each of these certificates has equal value, conditions and characteristics for the investors. In Costa Rica the SML defines the following types of investment funds: open-end or close-end financial funds, open-end or close-end non-financial funds, and mega investment funds.⁸⁹

5.2.2 Debt Securities

The SML states that debt securities with maturity less than 360 days must be issued as commercial paper. If maturity is 360 days or more, debt securities must be issued as bonds.⁹⁰

In the securities markets of Costa Rica, public bonds, mainly issued by the Treasury and the BCCR, represented about 92 percent of the total traded value in the year 2000. Most primary market placements of private debt instruments are traded in over-the-counter (OTC) markets. Financial sector issues dominate private issues that are actually traded in organized markets.

The Treasury (MH) and the BCCR share an auction mechanism for the placement of their securities in the market. However, the government also has some other facilities to issues its securities such as the Direct Placement of MH-BCCR securities, MH-only Auction and MH-only Electronic Window.

The securities offered by the Government are the following:⁹¹

Fixed-rate Debt Securities

These are traded in the MH-BCCR joint auction with the intermediation of a broker-dealer. They are placed according to the offered price (interest rate). The issuance is in series, interest rate is fixed and coupons are paid every six months. These securities are taxed with an 8 percent income tax. The minimum amount is ₡250,000 and these are medium term securities.

Once the auction has taken place (every Monday), the outcome is electronically published and two days later payment of the securities takes place. The issue may consist of individual securities or a global note.

Zero-Coupon Securities

These securities are in the market since September 1997. As with the fixed-rate securities, these are traded in the MH-BCCR joint auction with the intermediation of a broker-dealer. Zero-coupon securities are issued with a value date of two days after the auction took place. The investors offer the total amount as well as the discount rate and the issuance is assigned according to these parameters.

⁸⁹ Article 80 of the SML.

⁹⁰ Article 15 of the SML.

⁹¹ For further information see the website of Ministry of Finance (www.hacienda.go.cr).

Zero-coupon securities are standardized and are issued in series. There are only four maturity dates, despite the date of issue. They are placed at a discount, do not bear interest (zero-coupon) and the minimum amount is ₡250,000. Zero-coupon securities are also subject to an 8 percent income tax. These are issued only as global notes, although for very special cases individual securities may be issued.

These securities can be placed through MH-BCCR Joint Auctions, MH-BCCR placements not subject to an auction process and through MH-only Electronic Window (*Ventanilla Electrónica sólo MH*). The characteristics of the securities are identical in all three cases. However, the mechanisms differ in that in the last two investors only offer the amount, not the discount rate, which is predetermined. Moreover, the Electronic Window facility is reserved only for those public institutions under direction of the Budgetary Authority.

Variable-rate Securities (Basic Rate)

These securities were first issued in 1990. Their characteristics are substantially different from the other securities mentioned above.

The MH places these securities every month through the MH-only Auction mechanism. Securities are assigned according to the offered price (interest rate). Maturity may vary from medium to long term and the minimum amount is ₡1,000,000. The interest rate is equivalent to the Basic Rate for Liabilities⁹² plus a spread that is previously established. Coupons are paid every six months and the securities are subject to the 8 percent income tax.

All the above-mentioned securities are denominated in colones.

Variable-rate Securities in USD

These securities were first issued in March 1995. They are placed using the MH-only Auction with the intermediation of a broker-dealer. Investors offer both the amount and price. Interest rate is equivalent to the six-month LIBOR plus a previously agreed spread. Coupon is paid every six months and these securities are not subject to income taxes. The minimum amount is USD 5,000. The outcome of the auction process is published electronically the same day, although the value date is two days after.

Fixed-rate Securities in USD

These securities are placed using the MH-only Auction. The issuer fixes the interest rate and coupon is paid every quarter or every semester. These securities are also exempt from income taxes. The minimum amount is USD 5,000 and these securities are issued individually.

⁹² The Basic Rate for Liabilities is a weighted average built every week by the BCCR with information of the 6-month rates for liabilities reported by banks and financial firms.

Variable-rate Securities (TUDES)

These securities were first issued in 1993. The main feature of these instruments is that they are issued in Indexed Units (*Unidades de Desarrollo*, UD).⁹³

TUDES are issued in series through the MH Electronic Window. The minimum amount is USD 10,000, according to the value in colones at the moment of the purchase of the security. Coupon is paid every six month in colones, according to the value of the UD at that moment. Public institutions are the main buyers of these securities.

The securities issued by the Central Bank are the following:

Monetary Stabilization Bonds (BEMs)

BEMs are issued in colones by the BCCR, according to Article 61 of the LOBCCR. These securities are placed weekly (Monday or the next working day) together with the securities issued by the MH. Currently these securities are issued in series and there is a single maturity date for groups of four or five auctions. Maturities are one, three, six and twelve months. The minimum amount is 250,000 colones.

The BCCR issued other instruments in the past. Some of them are still in circulation:

- Zero-Coupon Global Note Bonds.
- USD-denominated Bonds issued in series.
- Colones-denominated Standardized Bonds issues in series.
- Colones-denominated Zero-Coupon Standardized Bonds issued in series.

5.3 SECURITIES IDENTIFICATION CODE

Nowadays in Costa Rica securities are not issued following a standardized coding. Each entity uses its own coding system.

A standardization process is currently underway. This process intends to assign identification codes that comply with the criteria of the International Securities Industry Numbering (ISIN).

5.4 TRANSFER OF OWNERSHIP

The transfer of ownership of securities immobilized at a central securities depository is made simply by book entries, that is, the transfer from one account to the other. There is no need for material delivery of the documents or for the proof of endorsement of the securities.⁹⁴

⁹³ The UD is an index calculated by SUGEVAL and is based on the change of the Consumer Price Index during the previous month. For more details see the SUGEVAL website (www.sugeval.fi.cr).

⁹⁴ Article 137 of the SML.

Regarding bearer and registered securities, in order to legitimize the rights stemming from them, the securities need to be endorsed in administration and delivered to the custodian so that the latter may be in a position to execute such rights. The entities that act as custodians have to provide their depositors with non-negotiable proof certificates in order for the latter to demonstrate ownership. In the case of registered securities these proof certificates will be used for registration purposes with the issuer in order to exercise the rights stemming from the securities.

For securities represented by book entries the transfer occurs with the inscription in the corresponding registry. The inscription of the transfer in favor of the buyer produces the same effects as the physical delivery of the securities. The person or firms that appears in the books of any of the entities comprising the Book Entry System (*Sistema de Anotación en Cuenta, SAC*) is regarded as the legal owner. Thus, these persons can demand that the rights stemming from the security represented by book entries be executed in their favor.⁹⁵

In order to legitimate the execution of the rights stemming from this last type of securities non-negotiable deposit certificates will be provided.

5.5 PLEDGE OF SECURITIES AS COLLATERAL

Article 19 of the SML states that issues may be collateralized with common instruments such as mortgages, pledges, guarantee trusts or commercial paper. These securities must be deposited in a financial entity controlled by the SUGEF or in a central securities depository (CSD). Several institutions having a special authorization may guarantee securities issues as well.

In Costa Rica, when physical securities (either immobilized or not) are pledged, the property rights are not transferred to the creditor. Therefore, the pledge cannot be executed directly without the order of a judicial court. On the other hand, for securities represented by book entries there is a special regime (Articles 115 to 125 of the SML). These securities are pledged by registering a lien in the corresponding account and the pledge is equivalent to the transfer of ownership of the security.

For physical and immobilized securities, the use of a trust fund is common since it reduces the legal uncertainty associated with the execution of the pledged securities. Article 648 of the Commercial Code states that a trust may be created over properties and rights pledged as collateral. In case of a default, for example, the fiduciary can sell these properties, according to terms agreed in the corresponding contract.

Repos

According to Articles 49 and 50 of the SML, a repo is a contract whereby one part (*reportado*) transfers the ownership of securities of a given type, at a certain price, to a counterpart (*reportador*). Once the agreed maturity of the transaction expires, the *reportador* is obliged to transfer back to the *reportado* the ownership of the same amount and type of securities against reimbursement of the established price. The accessory rights and the obligations related to these securities remain with

⁹⁵ Articles 123 and 124 of the SML.

the *reportado*. Any voting rights correspond to the *reportador*, except where a different agreement was made.

5.6 TREATMENT OF LOST, STOLEN, OR DESTROYED SECURITIES

Article 144 of the SML states that the depositors are responsible for the securities and for the validity of the transactions associated with them. For this reason custodians are not liable for defects, legitimacy or the nullity of the securities or of the transactions from which the securities originate.

Article 13 of the CEVAL's internal regulations establishes that in case of loss or destruction of the deposited securities the CSD will start the necessary procedures in order not to alter their ownership and will do anything in its power to replace them, according to the country's legal framework. The CEVAL will not be responsible for any damage caused by destruction or loss by reasons outside its direct control.

At present CEVAL has insurance policies in order to cover theft and robbery risks, assault and all others associated with its activities.

5.7 LEGAL MATTERS CONCERNING CUSTODY

In Costa Rica the securities custody service can be preformed only by companies called central securities depositories (CSDs), previously authorized by SUGEVAL and constituted with the sole purpose of providing the services authorized by the SML, as well as the brokers-dealers and those entities supervised by the SUGEF. The SUGEVAL is in charge of approving, supervising, and determining the security standards for securities custodies.

At present CEVAL is the only entity authorized as a CSD.

Articles 134 to 143 of the SML establish the legal framework for the securities custody function. These rules will be discussed in more detail in Section 6.2. Some specific legal aspects concerning custody are described below.

5.7.1 Protection of Securities Under Custody in case of Bankruptcy or Insolvency of the Custodian

Securities under custody are not considered as part of the assets of the custodian. The securities are neither considered part of the assets of the depositor itself when these have been deposited on behalf of a third party.

5.7.2 Fungibility

The SML established the obligation of standardization for issuers with the general objective of ensuring the largest possible volume of perfectly fungible securities. In this regard, Article 11 of the

ROPV establishes that to consider the securities of a single issuer as issued in series, they must have identical characteristics as for the face value, term and maturity. Moreover, standardized issue must have a minimum amount of a hundred million of colones and a minimum number of two hundred securities in order to ensure that the volume of securities is sufficient to give depth to the secondary market.

Currently, CEVAL depositors may hold deposit accounts of fungible securities, non-fungible securities or both. The fungible ones are those comprised of securities issued in series. The non-fungible ones are those comprised of individual securities.

Regarding securities represented by book entries, once the SAC system is operating all these securities will be fungible. The SUGEVAL will dictate the necessary regulations for this purpose.

5.7.3 Elimination of Physical Delivery

Custodians have to provide their depositors with non-negotiable certificates for the deposited securities in order for the latter to prove ownership. In the case of registered securities these proof certificates will be used for registration purposes with the issuer in order to exercise the rights stemming from the securities.⁹⁶

For securities represented by book entries, in order to prove the legitimacy of the corresponding rights a deposit certificate must be issued by one of the entities comprising the SAC system.

MARKET STRUCTURE AND TRADING SYSTEM

5.8 PUBLIC OFFERING OF SECURITIES

According to Article 2 of the SML, a public offering is defined as every offering, explicit or implicit, to issue, place, negotiate or trade securities that is transmitted to the general public or to specific groups by any means. Within this legal framework, the Regulations for the Public Offering of Securities (ROPV) considers a public offer the following:

- The offering of securities within the national territory through advertisement using the information media or communication channels that normally target the general public, such as television, radio, press and the Internet.
- The offering of securities within the national territory with similar characteristics to those of other securities already issued by the same issuer and for which the latter previously requested authorization for their public offering or those for which the SUGEVAL administratively determined the existence of a public offer.

⁹⁶ Article 138 of the SML.

- The offering of securities by brokers-dealers or any other entity subject to the control of the SUGEF, the SUGEVAL or the SUPEN.

On the other hand, the following are not considered a public offer:

- The offering of unregistered securities, according to Article 22 of the SML and within the limits established in the “Rules for the Trading of Securities Not Registered in the SUGEVAL” (*Disposiciones para la negociación de títulos o valores no inscritos en la SUGEVAL*), approved by the CONASSIF.
- The execution of purchase or sale orders by brokers-dealers of foreign securities in markets other than Costa Rica, according to the “Regulations for the public offering and trading of foreign securities and for the trading of foreign securities in markets other than Costa Rica” (*Reglamento para la oferta pública y negociación de títulos extranjeros y para la compra y venta de títulos extranjeros en mercados de valores diferentes al Costarricense*) approved by the CONASSIF.
- The offering of securities by foreign issuers executed through the Internet, as long as the issuer or the intermediary have clearly established that such an offering is not directed to the Costa Rican market and have taken reasonable measures to ensure that these securities will not be purchased in Costa Rica or by Costa Rican citizens.
- The offering of securities by domestic issuers issued in accordance with foreign laws, executed through the Internet, as long as the issuer or the intermediary, besides the conditions cited above, have established systems with access key or similar in order to avoid the access of Costa Ricans residents or citizens.

Entities Authorized to Execute a Public Offering of Securities

Article 2 of the SML states that issuers and brokers-dealers may execute a public offer of securities as long as these securities have been authorized for this purpose. Investment and pension funds managing firms may also execute a public offering of securities only in connection with the shares of the funds they manage. On the other hand Article 10 of the SML also authorizes the entities supervised by the SUGEF for the individual debt securities they issue as well as the State and non-banking public institutions.

5.9 PRIMARY MARKET

Securities issues can be placed in the primary market directly by the issuer or through a stock exchange. When the placement of an issue, or a portion thereof, through the stock exchange exceeds USD 1 million or its equivalent in colones according to the exchange rate determined by the BCCR, such a placement must be executed through an auction. In a day in which securities are placed through an auction it will not be possible to also place the securities directly among market participants.

Table 8: Total Traded Value in the Primary and Secondary Markets at the BNV
(in millions of colones and percentages)

	1998	1999	2000	2000 Jan-Jun	2001 Jan-Jun
Primary Market	2,591,816	2,489,909	1,988,650	1,098,291	955,875
Share (%)	54.2	38.9	26.5	29.3	19.9
Secondary Market	2,190,977	3,919,099	5,525,087	2,385,918	3,227,499
Share (%)	45.8	61.1	73.5	70.7	80.1
TOTAL	4,782,793	6,409,008	7,513,737	3,484,209	4,183,374

Source: BNV.

In year 2000 the total traded value in the primary market was of ₡1,988.7 billion, which represented a 20 percent decrease versus the value traded during 1999. At the same time, comparing the first semester totals for 2001 and 2000 the former registered a 13 percent decrease. In past years stock issues in the primary issuance showed little increments, from ₡39 billion in 1997 to ₡45.4 billion in 1999. Nonetheless, these issues represented less than 2 percent of the total traded value in the primary market.

5.10 SECONDARY MARKET

According to the SML, only those securities registered in the RNVI may be traded and be subject of public offer in the secondary markets.⁹⁷ Registration in the RNVI is a prerequisite for the authorization of public offering in the conditions determined in Articles 10, 15 and 17 of the ROPV.

In their internal regulations the stock exchanges must determine the additional requirements with which an issuer has to comply in order for its securities to be listed for trading in the secondary market. Stock exchanges must also establish the rules for the trading of securities in the secondary market.

With reference to the traded amounts in the Costa Rican markets, the secondary market has increased its share from 45.8 percent in 1998 to 73.5 percent in 2000. During the first semester of 2001 the trend continued with a share over 80 percent (see Table above).

In fact, the secondary market has been the growth driver in the total (primary and secondary) traded value in the stock exchange. Even with the decrease of the primary market's share, the total trade value rose by more than 17 percent in year 2000 compared to 1999. During the first semester of 2001 growth is close to 28 percent when compared to the same period for year 2000.

⁹⁷ Article 22 of the Law 7732. However, the stock exchanges themselves may execute transactions with securities not registered in the RNVI.

5.11 STOCK EXCHANGE TRADING

Stock exchange transactions are executed through different electronic trading platforms operated by the BNV.

The TEDEL system has been working since 1997. This is a trading system for spot and forward transactions and for repos. The system operates from 10.30 A.M. to 1.00 P.M. and has a settlement cycle of T + 1.⁹⁸

The “Liquidity Market” (*Mercado de Liquidez*) is a trading system for overnight repos with MH or BCCR securities. This system operates from 11.30 A.M. to 12.30 P.M. and settles in T.

The “SITE” system became operational only in Spring 2001. This system is designed for standardized securities and operates from 10.00 A.M. to 1.00 P.M. The settlement cycle is T + 3 for stocks and T + 1 for international bonds.⁹⁹

There is also a system called “Primary Auction” (*Subasta Primaria*) in which public securities are traded every 14 days and private securities, mainly short-term securities such as certificates of deposit issued by financial institutions, are traded daily. The system operates from 11.00 A.M. to 1.00 P.M. and settlement occurs in T + 2.

On the other hand, the BNV, through the *Instituto Centroamericano de Finanzas y Mercado de Capitales* (ICAF) operates the “Interbank Money Market” (*Mercado Interbancario de Dinero*, MIB).¹⁰⁰ However, the rules for this system are determined by the BCCR. Actually, only banks and the BCCR¹⁰¹ itself may participate in the MIB. Repos and outright loans with a maximum maturity of 30 days may be traded in the MIB. Settlement is gross, in real-time, and takes place on the reserve accounts the banks hold with the BCCR.

The MIB and the Liquidity Market systems have experienced significant increases in total traded value in the last years. These numbers are reflected in Table 9.

Finally, the BNV operates the MONED, the foreign exchange trading platform. This is a real-time gross settlement (RTGS) where transactions are settled on a Payment-versus-Payment (PvP) basis. The BCCR regulates and controls the clearance and settlement system of this foreign exchange market. Starting November 1998 transactions are settled through the SINPE.

⁹⁸ Until recently this system was settling in T.

⁹⁹ For the SITE system, the SUGEVAL has only approved trading of stocks and some international bonds, mainly eurobonds issued in USD in Costa Rica.

¹⁰⁰ The ICAF is a subsidiary enterprise of the BNV.

¹⁰¹ However, for the securities leg settlement the banks still require the custody services provided by the brokers-dealers.

Table 9: Total Traded Value in the MIB and Liquidity Market Systems
(in millions of colones)

	1999 Jan-Jun	2000 Jan-Jun	2001 Jan-Jun
Interbank Money Market (MIB)	77,984	158,381	621,305
<i>Total Amounts financed by the BCCR</i>	50,200	136,448	343,848
Liquidity Market	252,875	386,835	536,810
<i>Colones</i>	174,330	256,340	369,606
<i>USD^(a)</i>	78,545	130,495	167,204

Source: BCCR.

^(a) Amounts transformed to colones at the average exchange rate of every year.

5.12 OVER-THE-COUNTER MARKET (OTC)

The OTC market in Costa Rica is limited in practice by Article 23 of the SML, which states that buy and sell transactions and repos of publicly offered securities must be executed through the respective members of the stock exchange (i.e., the brokers-dealers). Thus, the OTC market is limited to issues of individual bonds made by institutions supervised by the SUGEF.

In July 1999 the CONASSIF approved a Regulation for the buying and selling, repos and repurchase of publicly offered securities outside the stock exchange. This regulation determines that the stock exchanges may authorize that these transactions be performed outside its normal trading systems in the following cases:

- Transactions resulting from a public buyout, in accordance with the corresponding regulations.
- b. Transactions directly related to mergers, spin-offs or those that originate from the reorganization of the relevant firm.
- c. Transactions with securities whose trading in the stock exchange has been suspended.
- d. Transactions with securities issued by firms that have been intervened because of a court order.
- e. Transactions authorized by the Superintendent of the SUGEVAL for those cases where it can be demonstrated that trading at the stock exchange could originate distortions in the market price of the corresponding securities.

In all these cases, the purchases, sales and repos must be executed through an authorized broker-dealer. Publicly offered securities that are purchased with a purpose other than trading, executing repos or repurchases do not necessarily have to be performed at the stock exchange, although the SUGEVAL must be informed of such transactions. This obligation falls to the buying broker-dealer,

who has to inform the SUGEVAL and the stock exchange on the transaction it carried out. As a minimum, the communication must contain the identification of the relevant securities, traded volume and traded amount, acquisition price and the exception that justifies the transaction being performed outside the stock exchange.

Stock exchanges must inform the public of all transactions that have been executed through means different than the normal trading systems. The Superintendent of the SUGEVAL sets the time frame (no later than five days) and the means for the stock exchange to publicize this information. Additionally, stock exchanges must have a record of these transactions and ensure that the general public is informed through the same channels as for ordinary (stock exchange) transactions.

5.13 MARKET SIZE

The total traded value (primary and secondary market) in the BNV for the first semester of 2001 reached ₡183,374 million, 20 percent more than the value for the same period of 2000. The secondary market has been increasing its share in the total with more than 80 percent of the total traded value during the first semester of 2001 (see Table 8). Stock market capitalization as of March 2000 was ₡717,154 million.

Table 10 shows the recent evolution of the Costa Rican market regarding transactions with private versus public securities, colones versus dollars and short versus long term. The general trends are a stable and significant predominance of the public sector, an increasing share of USD denominated securities and the relative increase of securities with maturity over 180 days

Table 10: Traded Amounts at the BNV According to Sector, Currency and Maturity
(in millions of colones and percentages)

	1998	1999	2000	2000 Jan-Jun	2001 Jan-Jun
Public Sector	4,325,182	5,903,385	6,915,538	3,258,059	3,766,357
Share (%)	90.4	92.1	92.0	93.3	90.0
Private Sector	457,610	505,623	598,199	226,150	417,017
Share (%)	9.6	7.9	8.0	6.7	10.0
Colones	3,092,324	3,159,660	3,172,394	1,707,769	1,702,480
Share (%)	64.7	49.3	42.2	49.0	40.7
USD	1,690,469	3,249,347	4,341,344	1,776,440	2,480,894
Share (%)	35.3	50.7	57.8	51.0	59.3
Maturity: < 180 days	4,377,285	5,176,955	6,115,381	2,848,970	3,110,093
Share (%)	91.6	80.8	81.4	81.8	74.3
Maturity: > 180 days	403,515	1,232,050	1,398,356	635,238	1,073,281
Share (%)	8.4	19.2	18.6	18.2	25.7

Source: BNV.

6 CLEARANCE AND SETTLEMENT CIRCUITS FOR GOVERNMENT AND CORPORATE SECURITIES

6.1 ORGANIZATIONS AND INSTITUTIONS

6.1.1 Stock Exchange

The Regulations of the *Bolsa Nacional de Valores* (BNV) establish that stock exchange transactions executed by brokers-dealers must be settled using the mechanisms and in the venue established or authorized by the stock exchange. The BNV may establish separate settlement procedures depending on the nature of the transaction and it may maintain different locations for settlement to take place.

These Regulations also establish that the BNV will operate as a clearinghouse for the transactions performed through it. To this purpose, it will establish the necessary arrangements and necessary mechanisms in order to create and operate clearing systems or procedures.

The BNV has established a CSD to carry out these duties.

6.1.2 Central Securities Depository

The CEVAL is at present the central securities depository (CSD) of the Costa Rican securities markets and it executes most of the clearance and settlement operations. The functions of CEVAL are the following:¹⁰²

- Receive securities in deposit from financial intermediaries as well as those comprising the portfolios of mutual funds.
- Administrate the securities received in deposit (collection of the repayment, coupons and dividends).
- Clear and settle transactions related to the deposited securities.
- Issue pledge certificates over the deposited securities, if required by the depositors.
- Issue and manage multiple or global notes.

The CEVAL acts as the clearing and settlement member for the securities leg of transactions made at the stock exchange. Securities are settled gross, while the cash leg is settled on the reserve accounts participants hold at the BCCR.

¹⁰² Article 96 of the BNV regulations.

Participants in the CEVAL are brokers-dealers, issuers with securities listed in the BNV, investment funds managing firms and all the other persons, firms or contracts authorized by the BNV for this purpose.

The types of transactions that issuers and depositors make through the existing trading systems and that are cleared by the CEVAL are the following:¹⁰³

- Term (*A plazo*).
- Put and Call Options.
- Ordinary Spot Transactions (those that must be settled no later than the next working day following the trading day).
- Same-day Spot Transactions (those that must be settled during the same day in which trading took place).
- Forward (*A futuro*).
- At Premium.
- Others authorized by the BNV.

As of June 2001 the balance of securities deposited at the CEVAL was approximately ₡1,600 billion (USD 5,270.2 million, see Table 11). So far, global notes are being used as a means to facilitate securities trading and settlement. Nearly 68 percent of the debt securities (including 98 percent of international bonds) and 53 percent of stocks (including 100 percent of international stocks) were immobilized. The CEVAL has vaults both at its headquarters in the capital city of San Jose (located in the building of the *Banco Crédito Agrícola de Cartago*), and in the *Banco Nacional de Costa Rica*.

6.2 SECURITIES REGISTRATION AND CUSTODY PROCEDURES

6.2.1 Registration in the RNVI

All the natural and legal entities who directly or indirectly participate in the securities market, except for investors, as well as the actions and contracts referring to this market and the securities issues that are publicly offered must be registered in the National Registry of Securities and Intermediaries (*Registro Nacional de Valores e Intermediarios*, RNVI). The SUGEVAL manages the RNVI through a specialized department. The general public has access to the information available in the RNVI.

The Regulations of the RNVI establish that the following shall be registered: securities issuers and their issues, stock exchanges, brokers-dealers and their agents, investment funds managing firms

¹⁰³ Article 68 of the BNV regulation.

Table 11: Securities Deposited at CEVAL
(in USD million)

	<i>Dec-1999</i>	<i>Dec-2000</i>	<i>Jun-2001</i>
Balance of Domestic Securities	3,228.9	3,713.3	4,475.8
Balance of International Securities ^(a)	385.6	645.8	794.4
TOTAL	3,614.5	4,359.1	5,270.2

Source: CEVAL.

^(a) Balances maintained through international custodians.

and their funds, risk rating agencies, central securities depositories, custodians, clearing and settlement firms, settlement agents, financial groups, and any other natural or legal person participating in the securities market whose registration is required by the Superintendent of the SUGEVAL. Additionally¹⁰⁴, compulsory and voluntary pension funds, work capitalization funds and voluntary savings funds must also be registered in the RNVI. Neither the issuer may place its securities nor any other entity may perform its corresponding activities if not properly registered with the RNVI.

Regarding the entities subject to registration, the following actions must be registered:

- Authorization for the public offerings of securities or services.
- Authorization for public buyouts.
- Authorization for the constitution of financial groups.
- Authorization for the modification of the above-mentioned actions.
- Suspension of the authorization for public offerings of securities or services.
- Revocation of the authorization for public offerings of securities or services.
- Precautionary measures.
- Applied sanctions, with the exception of private rebukes.¹⁰⁵
- De-listings.

Supporting documentation and updates must also be provided. Additionally, the records of each entity must include the periodical information that they are compelled to provide by law.

¹⁰⁴ In the case of those funds subject to the authorization of the SUPEN, the RNVI will only register the corresponding authorization agreement.

¹⁰⁵ After 10 years the applied sanctions are deleted from the Registry.

6.2.2 Registration and Custody of Securities

The deposit with custodians is constituted with the delivery of the securities, or, if applicable, with the corresponding book entries. Securities deposited with the same custodian are transferred from one account to the other together with the corresponding registries. There is no need of physical delivery of securities or to exhibit endorsement certificates. In the case of deposits of bearer and registered securities the securities need to be endorsed in administration and delivered to the custodian.

Custodians have to provide the depositors with non-negotiable certificates of the deposited securities, which enable the latter to demonstrate ownership.

6.2.3 Registration and Custody of Securities in the CEVAL

In order to be a depositor with the CEVAL, the authorized entities must present a written application together with a notary certification of the constitution act of the company. The CEVAL evaluates these applications and decides on whether or not to admit the applicant.

Only securities and bonds explicitly accepted by the CEVAL and published in its official listing may be deposited.

The deposited securities must be of valid delivery, authentic and in perfect physical condition, with no expired coupons. They should not be subject to any seizure actions or administrative processes or legal orders that could alter the exercise of ownership, legitimacy or circulation. Depositors are responsible for the authenticity of the securities, their legal existence and for their rights over the securities.¹⁰⁶

Bearer securities need to be blankly endorsed, while for the registered ones, in addition to the correspondent endorsement the depositor needs to make sure that the securities have been registered in the issuer's registry.

6.2.3.1 Deposit Accounts

Once the deposit contract has been signed, the CEVAL assigns deposit accounts that may be of a fungible (integrated by securities issued in series), non-fungible (integrated by individual securities) or mixed nature. A single number per custodian identifies depositors' accounts. Using this single number depositors have access to their registries at the CEVAL.

6.2.3.2 Transactions Execution

CEVAL executes all the instructions received from its members as long as they are in line with Costa Rican laws, regulations and the CEVAL's own policies. Individual instructions need to be sent for

¹⁰⁶ The CEVAL must revise those securities received in deposit and will be responsible, together with the depositor, when these contain evident and clear defects.

every type of transaction or movement using a single and uniform structure of forms. The latter must be transmitted through the channels accepted by the CEVAL: electronic media that the CEVAL make available to its customers, fax, telex, certified mail or direct delivery at the CEVAL's reception counters.

With the purpose of keeping control over the validity of the provided information, the CEVAL requests of its customers a signature registry endorsed by a Notary Public. The registry must include the signatures authorized for issuing instructions as well as those authorized for making withdrawals of securities and/or coupons. Depositors are fully responsible for updating this registry.

The CEVAL must carefully examine the information received from the participants. Once this is done it executes the instructions. The CEVAL registers in depositors' accounts all the incoming and outgoing movements of securities indicating the date, amount, securities identification and any other information considered necessary. The CEVAL does not keep the securities of its customers as part of its own assets and for accounting purposes these are considered as off-balance sheet items.

6.2.3.3 Deposit Account Information

The CEVAL provides information on the deposited securities to users through electronic media or through periodic reports. For every security entered in their own account, depositors receive a global custody certificate. Those clients connected to CEVAL's system can print a Daily Movement Report, which includes the details of the movements during the day. The CEVAL also provides depositors with monthly statements.¹⁰⁷

6.2.4 Securities Withdrawal

When a deposit expires, the custodian is compelled to return to the depositors securities of the same issuer, same species and same characteristics of the deposited ones. When bearer or registered documents are withdrawn, the effects of the endorsement in administration cease. The custodian will endorse them again to the depositors requesting the withdrawal with no further responsibility.

6.3 GUARANTEE SCHEMES

According to Article 78 of BNV Internal Regulations for the settlement of stock exchange transactions, the brokers-dealers have to ensure that settlement will take place under all circumstances with the guarantees they have created for this purpose, which may include their own equity. With anticipation and on a generalized basis the BNV can also demand that brokers-dealers provide collateral for some types of transactions they execute on behalf of their clients or for transactions associated with asset management for third parties.

To ensure that the settlement of the cash leg takes place, brokers-dealers are required to have a bank credit line of at least ₡50 million (about USD 150,000). There is also a settlement fund in which

¹⁰⁷ It is also possible to request partial account statements (i.e., for a time period shorter than one month) at an additional charge for the client.

every broker-dealer must make a \$5 million contribution. This fund is not mutualized, i.e., in case of a default only the contribution of the defaulting party may be used ("defaulter pays" scheme).

Article 82 of the BNV Internal Regulations sets the mechanisms of "Contract Resolution" and the "Coercive Execution" for default situations in stock exchange transaction settlement. These mechanisms are described in detail in Section 6.4.4.

6.4 SECURITIES CLEARANCE AND SETTLEMENT PROCESS

6.4.1 Legal Aspects Concerning Securities Clearance and Settlement

Article 130 of the SML states that the securities clearance and settlement system has to follow the principles of universality, delivery versus payment (DvP), objectivity of the settlement date, delivery assurance and financial neutrality. These principles are specified in the following statements:

- a The system will be integrated and will admit as few specialties as possible. All stock exchange transactions will be settled through it.
- b Securities and cash transfers resulting from a settlement will be executed simultaneously through the system
- c The settlement for each stock exchange session will take place in a pre-established number of days. The time span between the trading sessions and the settlement date will always be the same for each type of transaction and as short as possible.
- d The system will provide mechanisms to ensure that the settling creditor members will have at their disposal the cash or the securities on the settlement date. For this purpose it will borrow or even buy the corresponding securities.
- e The securities clearance and settlement system will be neutral in financial terms. The debits and credits in the cash account held at the BCCR by every clearing member or at the designated settlement bank will have to be executed with same day value.

In case of lack of sufficient balances in the corresponding accounts the clearance and settlement system must determine formulas to ensure that settlement will occur, charging the guarantees determined by the SUGEVAL.

6.4.2 Settlement Modalities

As mentioned in section 5.11, the stock exchange transactions are executed using different trading systems. For each of these there is a different settlement scheme:

- The "TEBEL" system in which spot and forward transactions and repos are traded has a settlement cycle of T + 1.

- In the “Liquidity Market”, for very short-term repos, the settlement occurs in T.
- In the “SITE” system, designed for standardized securities, the settlement cycle is T + 3 for equities and T + 1 for international securities.
- In the “Primary Auction” system settlement cycle is T + 2.

For all these systems every day a single multilateral net position is calculated for the cash leg, which then settles on the reserve accounts maintained by the intermediaries at the BCCR. On the other hand, the securities leg is settled on a gross basis on the accounts held at CEVAL by brokers-dealers.

On the other hand, for the case of the interbank money market (i.e. the MIB system), settlement is gross and in real time, and takes place in the CEVAL securities accounts and in the cash reserve accounts held at the BCCR.

CEVAL does not act as a central counterparty for any of the above-mentioned trading platforms and its system is not integrated with the SINPE, through which the BCCR handles the reserve accounts of the intermediaries.

6.4.3 Settlement Procedures

6.4.3.1 *TEBEL, Liquidity Market, SITE and the Primary Auction*

Trading in the various BNV platforms (TEBEL, Liquidity Market, SITE and Primary Auction) occurs at different hours.

TEBEL:	from 10.30 a.m. to 1.00 p.m.
Liquidity Market:	from 11.30 a.m. to 12.30 p.m.
SITE:	from 10.30 a.m. to 1.00 p.m.
Primary Auction:	daily from 11.00 a.m. to 1.00 p.m. for private securities and every 14 days for public sector securities.

In the TEBEL and the Liquidity Market systems, once a broker-dealer inputs into the system a securities selling offer, the securities are blocked by the CEVAL. That is, securities are blocked even before trade matching occurs. In the SITE system, on the other hand, securities are not blocked before trade matching. However, in the latter the delivery of securities is done manually. Thus, settlement of the securities leg is not circumscribed to a fixed period.

Settlement on Value Date: Calculating Balances

For the cash settlement starting from 1.00 p.m. CEVAL calculates a single multilateral net position for the four systems.¹⁰⁸ Thus, in day T the cash multilateral net position is the result (sum) of the following:

¹⁰⁸ The trading systems of the BNV are integrated with the CEVAL's systems.

- TEBEL position (debit or credit) resulting from transactions performed in T-1.
- Liquidity Market position (debit or credit) resulting from transactions performed in T.
- SITE position (debit or credit) resulting from transactions performed in T-3 for equities and in T-1 for international securities.
- Primary Auction position (debit or credit) resulting from transactions performed in T-2.

Securities are gross settled in the CEVAL deposit accounts.

Settlement on Value Date: Cash Settlement

At 2.30 p.m. of day T (value date) the cash multilateral net positions are settled using the Electronic Funds Transfer System of the SINPE (i.e. the TEF) on the BCCR reserve accounts.

Some of the brokers-dealers hold accounts with the BCCR while others use banks to settle, via the TEF, their obligations and those of their clients. In the majority of the cases the brokers-dealers that do not hold an account at the BCCR are actually part of a financial group and they use the SINPE through the group's bank. The SINPE Regulations state that starting January 1st, 2002 all financial entities will participate directly in the SINPE, same thing for every entity holding a reserve account at the BCCR.

Settlement on Value Date: Settlement of the Securities

At 4.00 p.m. of day T, the CEVAL registers in the depositor's account the securities inflows and outflows, indicating date, amount, securities identification and other information.

6.4.3.2 MIB

The MIB operates from 8.00 a.m. to 5.00 p.m. The MIB system is interconnected with that of the CEVAL.¹⁰⁹

In the MIB only banks and the BCCR may participate. In this system, once a participant inputs an offer the corresponding securities or cash are blocked in the CEVAL (the "MIB's free account") and the BCCR accounts respectively.

In case of an outright loan once the trade is matched the cash leg is settled gross in real time. The BCCR credits the account, via the TEF, of the borrowing bank and charges that of the creditor bank.

In case of repos, the underlying securities are transferred by the CEVAL to an account known as "MIB's pledge account".

As noted earlier, in Costa Rica repos are actually known as "repurchases" (*recompras*). Repurchases are a particular type of repo in which the underlying securities are deposited as collateral in a trust account created for this specific purpose: the "MIB's pledge account". In this regard, although banks

¹⁰⁹ As previously mentioned, this system is property of the BNV and operated by it.

can act as custodians, the delivery of the securities occurs using the accounts of the brokers-dealers. It is expected that with the SAC system banks will deliver the securities directly on their accounts.

6.4.4 Procedures in Case of Non-fulfillment of Obligations

For the operations executed through the BNV systems, in case one of the brokers-dealers does not fulfill its obligations within the established terms, the counterpart may request the coercive execution of the transaction or contractual resolution within four days following the non-compliance.¹¹⁰

6.4.4.1 Contractual Resolution

Once the contract resolution is requested the BNV ceases the corresponding transaction and returns to the fulfilling party what the latter had paid or delivered. The fees generated by this transaction are charged to the unfulfilling broker-dealer in addition to the sanctions established by the Law and the BNV's regulations.

6.4.4.2 Coercive Execution

In case of a default on the settlement of the cash leg, the BNV through a rotating system designates a broker-dealer¹¹¹ who in turn will choose a stock exchange agent to sell the delivered securities on behalf of the defaulting party. The sale needs to be executed at the best price on the day determined by the BNV. The resulting sale amount (less the fees of the designated selling broker-dealer) is delivered to the original selling broker-dealer. The defaulting broker-dealer must provide for all damages and losses resulting from this transaction. The amount of the indemnification is obtained by applying the interest rate currently paid by the *Banco Nacional de Costa Rica* on six-month deposit certificates to the amount of the transaction from the day of the default until the day the selling broker-dealer gets paid. If the amount stemming from the sale is insufficient to cover this indemnification, the BNV issues a credit note in favor of the original selling broker-dealer.

In case of a default on the delivery of the securities, the BNV through a rotating system orders a broker-dealer to purchase, on behalf of the defaulting party, the necessary securities to comply with the transaction. The purchase must be a same-day spot transaction at the best possible price on the day the BNV requests.

The transaction is paid with the funds that the fulfilling broker-dealer provided in the beginning. If this amount is insufficient the BNV will execute the guarantees provided by the defaulting broker-dealer until the obligation and the correspondent fees have been satisfied. If it has not been possible to purchase the securities in three stock market sessions, the BNV will return the paid amount to the original purchasing broker-dealer together with a credit note. The amount of the credit note will be determined by a third designated broker-dealer who will issue a quotation of the securities which

¹¹⁰ If within the stipulated term the affected counterpart has not expressed its will regarding these options the BNV will presume that the former is seeking for the coercive execution of the transaction and will act accordingly.

¹¹¹ In the rotating system neither the defaulting broker-dealer nor the one requesting the coercive execution are included.

are the object of the unfulfilled operation. If the quotation value is higher than the originally price the credit note will be issued for this difference plus the correspondent delinquency interest.

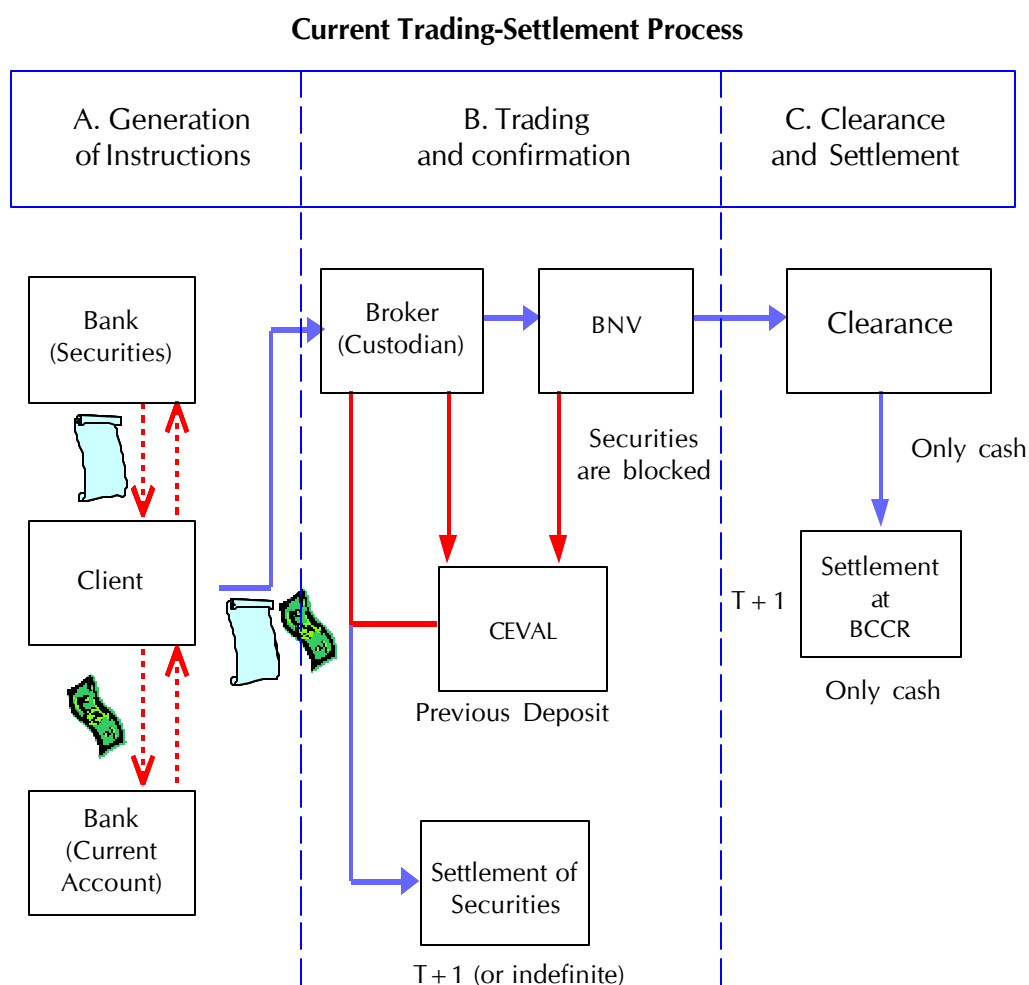
6.5 SECURITIES LENDING

Article 130, paragraph D, of the SML states that the clearance and settlement system will provide mechanisms to ensure that the settling creditor members will have at their disposal the cash or the securities on settlement date. For this purpose it will borrow or even buy the corresponding securities.

Currently in Costa Rica there is no automatic securities lending / borrowing facility.

6.6 FLOW CHARTS OF CURRENT SETTLEMENT PROCESSES

Figure 16: Current Settlement Process for Transactions Made at the BNV
(TEBEL and SITE systems)



Source: SUGEVAL.

Chart Explanation

- A. Before any transaction takes place the client must deliver to the broker-dealer the corresponding securities or funds (in cash or cheque). Thereby, the client previously withdraws the asset from the entity where it was deposited and transfers it to the broker-dealer that will handle the trade.
- B. In a securities purchase the broker-dealer previously deposits the funds in a current account it has with a settlement bank. In case securities are to be sold the broker-dealer must previously deposit the securities with the CEVAL.

Then the broker-dealer inputs the buy or sell offer in the trading systems of the BNV. In case of a sell it must indicate the deposit number of the securities intended for trading. In the TEBEL system the securities are blocked from the moment in which the broker-dealer inputs the transaction into the system. In the SITE system the securities are blocked once the trade has been matched.

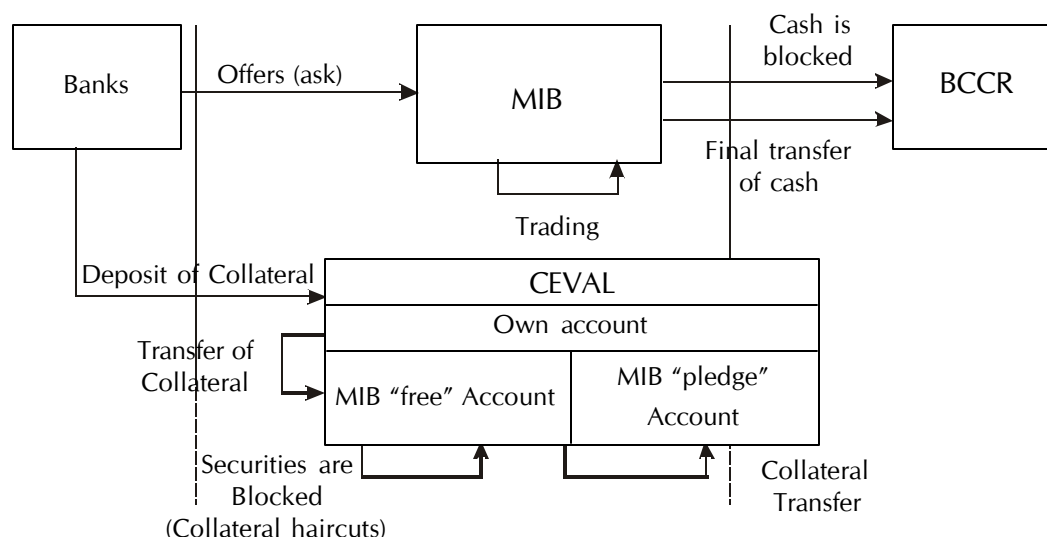
- C. In trading day (T) the BNV clears all the transactions held at the stock exchange on that day and send a file to the SINPE with the multilateral net cash positions.

The broker-dealers holding an account in the SINPE and the banks acting as settlement agents for the cash leg for broker-dealers that do not have an account in the SINPE know their cash positions on T. However, settlement does not take place until T + 1.

The multilateral net cash balances to be settled on that day (T + 1) include the outcome of the transactions held at the BNV on T (TEBEL and trading of international securities on the SITE system), the transactions made on T + 1 in the Liquidity Market, the equities transactions made on T-2 in the SITE and the transactions held on T-1 in the Primary Auction system.

Regarding securities deliveries, at 4:00 p.m. on T + 1 the CEVAL registers on the depositors' accounts securities inflows and outflows. If the delivery of securities is to be made manually (the case for the SITE system), transfers may occur on T + 1 or on any other day thereof until the selling broker-dealer is able to deliver the securities to its counterpart.

Figure 17: Current Process for the Bilateral Settlement of Transactions Made in the MIB system



Source: SUGEVAL.

Chart Explanation

1. Before any trading takes place the banks wishing to trade in the MIB must deposit with the CEVAL the corresponding securities. The securities are first deposited in their own accounts and then transferred to an account called "MIB free".
2. Once the securities are deposited in the "MIB free" account, the banks may input their offers into the trading system. From this moment securities are blocked by the CEVAL and cash is blocked by the SINPE.
3. Matched trades are settled on real time through the SINPE. If the transaction consists of outright loans the SINPE transfers the final funds balance from the creditor to the borrower. In the case of repos, funds are credited to the "reportador" and the CEVAL transfers the underlying securities to an account called "MIB pledge".

6.7 MAJOR PROJECTS AND POLICIES BEING IMPLEMENTED CONCERNING CUSTODY, CLEARING AND SETTLEMENT

As previously stated, the secondary market has significantly increased its share in the total traded value. An important element behind this is the standardization process, which has enabled investors to have access to more and better information owing to the standardization of amounts, maturities and interest rates.

The standardization process itself received a boost from the 1998 SML. In Article 10 the SML states that only those securities issued in series conforming to the rules determined by the SUGEVAL may be authorized for public offer in the primary market. The SUGEVAL has established the characteristics for securities of the same issuer to be considered as issues in series. This includes identical characteristics in terms of issuing date, face interest rate, face value, periodical coupon payments, maturity, currency denomination and Circulation Law, among others. Moreover, the ROPV determines that standardized issues must have a total minimum amount of a ₡100 million, or its USD equivalent, and a minimum of two hundred securities.

In addition to this, the relevant authorities of Costa Rica are working on a project called "Book Entry System" (*Sistema de Anotaciones en Cuenta, SAC*), in order to improve the current securities clearance and settlement system. The SAC might actually become the new CSD. It will have an open architecture that, in principle, will enable transactions with all kinds of securities, including equities.

The SML allocates the responsibilities for the SAC project to both the BCCR and the SUGEVAL. The SUGEVAL is in charge of setting the rules for the organization and the operation of the registries, the identification system and the control of securities represented by book entries. The BCCR is in charge of managing the registry of the issues of the State and of other public institutions.¹¹²

The registry of the securities registered in the RNVI and represented by book entries will be carried with a two-tier system. The first level will become the sole National Book Entry Registration System and will be created according to the rules determined by the SUGEVAL. It will be integrated by the CSDs authorized by the SUGEVAL that will manage the registry of private issues, and the BCCR who will manage issues of the State and public institutions. The second level will be formed by those entities joining the National Book Entry Registration System, i.e., the entities authorized to provide custody services and the settling members of the National Securities Clearance and Settlement System.

The work around the SAC project is organized in three main projects: i) the provision of new services by banks; ii) segregation of accounts; and, iii) management of settlement risk.

It is expected that banks will be able to offer custody and clearance services without having to go through a broker-dealer's account. At present banks can perform custody, but the delivery of the securities must be done using brokers-dealers' accounts due to the existing limitations in the CEVAL's system that does not allow the delivery to be made directly by the custodian. Thus, it is expected that once they become fully operational within the CEVAL, any custodian will be able to receive and deliver securities directly.

With reference to account segregation, Article 118 of the SML states that member institutions of the National Book Entry Registration System must maintain two accounts for every participating entity:

¹¹² The SML empowers the BCCR to delegate, totally or partially, the management of this registry to other members of the National Book Entry System.

one for their own account and the other for their clients. The SUGEVAL and the CEVAL are reaching agreements and measures in order to better regulate the segregation of the resources of the brokers-dealers and those of their clients.

Finally, regarding the improvements in settlement risk management some of the most important measures are the following:

- Trading and settlement will be strictly separated. Moreover, there will be an explicit distinction among clearance (calculation of the multilateral positions) and settlement. The stock exchange will be responsible for the clearance and risk management of the clearance process, while the SAC will be responsible for the settlement of multilateral positions, both for the securities and cash legs, on a DVP basis.
- The new system will have two separate DVP mechanisms, one for the net settlement of transactions executed at the BNV (DVP model 2) and the other for the real time gross settlement of securities transactions in the MIB market (DVP model 1).
- In order to ensure a true DVP for both mechanisms, the SAC will be connected with the RTGS¹¹³ system of the SINPE.
- For the interbank money market the SAC will give more flexibility since it will settle not only those transactions performed through the trading platform (the MIB) but also direct bilateral transactions and those executed through a broker-dealer.
- The SAC will operate with a settlement fund to be created and managed by the BNV. It will also have other similar measures to ensure that settlement of multilateral positions stemming from stock exchange transactions will take place.

¹¹³ This system is called Interbank Settlement System (*Sistema Interbancario de Liquidación*, SIL).

6.8 FLOW CHARTS OF FUTURE SETTLEMENT PROCESSES (SAC)

Figure 18: Future Settlement Process for Transactions Made at the BNV

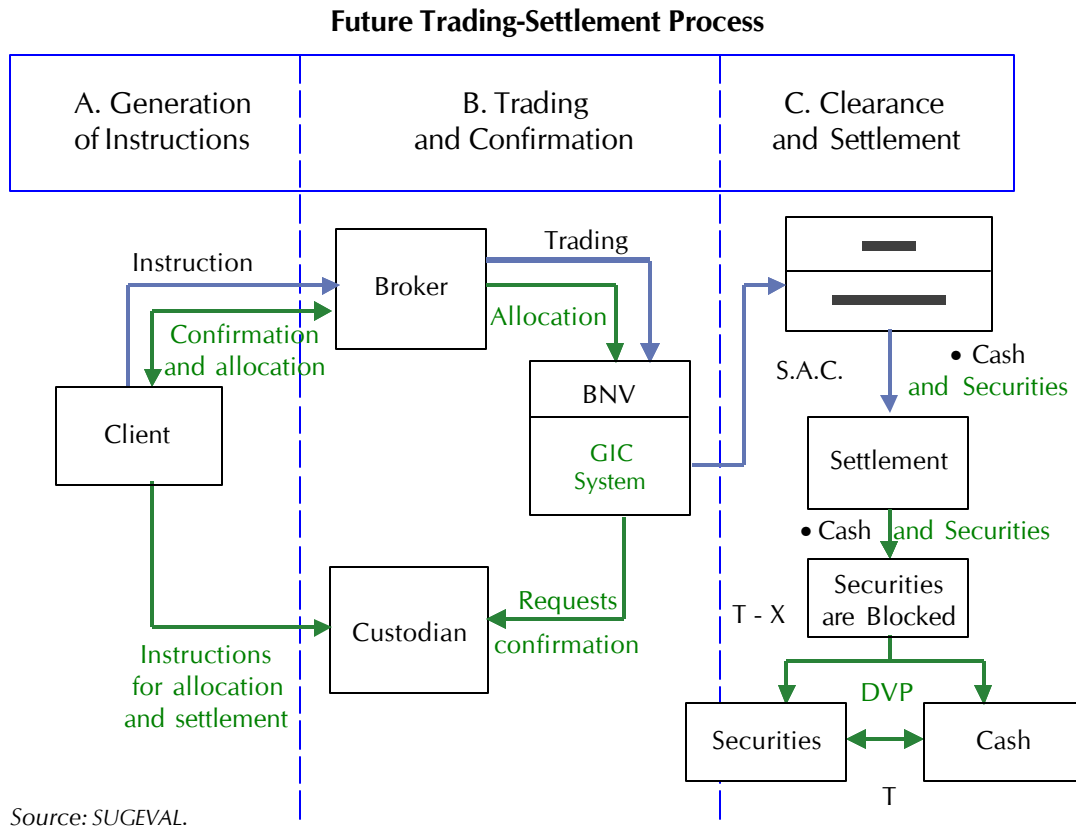


Chart Explanation

- A. The client sends buy or sell instructions to the broker-dealer. The latter groups the received instructions and executes the trades at the BNV.

The broker-dealer informs the client on the outcome of the trades and then the client informs the broker-dealer on how he wants to allocate matched trades. The latter information is sent by the broker-dealer to the stock exchange's system for instruction management (*Sistema de Gestión de Instrucciones*, GIC).

- B. If the broker-dealer is also the custodian of the relevant securities the GIC considers the allocations as confirmed. If the custodian is other than the broker-dealer, then the client must also inform the former on the desired allocations since the GIC will ask the custodian for confirmation of the allocations that the broker-dealer is indicating.

In the case of cash, if the broker-dealer does not hold a reserve account at the BCCR, then the GIC will ask its settlement agent for confirmation. 1.1

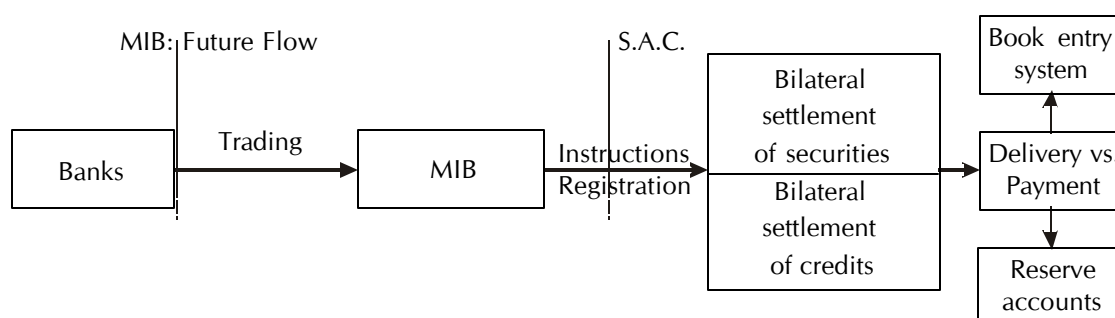
1.2

Once all allocations have been confirmed the GIC proceeds with clearance. The GIC generates a file with net cash balances and transmits it to the SAC. The SAC is actually in charge of the settlement on a DvP basis.

The day before settlement date (T-X), the SAC verifies the existence of the securities in the securities accounts and it may only block them if this is required by the BNV as part of its risk management processes.

On day T the SAC sends to the SINPE the information for the settlement of the cash leg. Once the SINPE confirms that all requested movements on the reserve accounts were successful, the SAC immediately makes the corresponding movements on the securities accounts.

Figure 19: Future Process for the Bilateral Settlement of Transactions Made in the MIB System



Source: SUGEVAL.

Chart Explanation

In the future banks will be able to make repos, outright loans and any other transactions for which they receive authorization by the BCCR. Settlement will occur on real time or deferred. If the transactions are made through the MIB, this system will send the corresponding information to the Securities Bilateral Settlement Module or to the Loans Bilateral Settlement Module of the SAC.

The SAC will begin with the settlement process according to the settlement date and time that have been indicated in each contract. The SAC send the SINPE the information on the movements to be made to the reserve accounts. Once the SINPE confirms that these movements were successful, the SAC will proceed with the corresponding movements to the securities accounts.

6.9 DERIVATIVES CLEARANCE AND SETTLEMENT

Although the SML includes various references to the derivatives market, transactions in this market are negligible as of current date. Article 43 states that futures market transactions are receivable in the day agreed-on in the contract and that all of them will have the same expiration date. The regulations of the stock exchanges will establish the margins that parties will have to deposit with the brokers-dealers in order to be able to perform futures contracts and maintain their position. Regarding settlement, Article 128 only states that the SUGEVAL will be able to authorize and control the settlement of derivatives market transactions.

6.10 INTERNATIONAL LINKS AMONG CLEARANCE AND SETTLEMENT INSTITUTIONS

In order to allow domestic investors to access international markets and deposits, the CEVAL maintains accounts with Clearstream and Deutsche Bank – Euroclear. On the other hand, the CEVAL maintains custody of foreign securities. As of June 2001 the latter securities amounted to USD 794.4 million, representing about 15 percent of the total amount held in custody by this entity.

7 THE ROLE OF THE CENTRAL BANK IN CLEARANCE AND SETTLEMENT SYSTEMS

7.1 RESPONSIBILITIES

In Costa Rica the central bank is the principal axle of the payments and securities clearance and settlement. As previously mentioned, the LOBCCR brings together all the legal elements that make the BCCR capable of organizing, operating, controlling and overseeing the payments system. Article 2 of the LOBCCR states that one of the targets of the institution is to promote an efficient domestic and external payments system and maintain continuity in its operation. Article 3 states that among the essential functions of the BCCR are the implementation, operation and oversight of the clearance system. Moreover, Article 69 gives the Board of Directors of the BCCR the responsibility of organizing and regulating the payments system.

The BCCR undertakes the following specific roles regarding the payments system:

System Developer: the BCCR is the creator of the technological platform known as the SINPE, which facilitates the provision of payment services.

Operator: the BCCR is the institution that operates and controls the electronic services, including the payments clearance and settlement functions.

Participant: just as any other participant, the BCCR handles its economic transactions through the SINPE.

Regulator and Overseer of the System: The rules and regulations governing the payments system are issued by the BCCR. Moreover, it is in charge of overseeing the system operation, to maintain its stability, efficiency and security.

With reference to this last role, besides the Regulations for the Payments System a set of regulations for various general and specific aspects of this service, including the technical, operational and functional areas has been created. These documents integrate what is called the “Blue Book” of the Payments System. The documentation is structured in series, each one with a number between 01 and 99 and one additional digit that identifies a particular book. For example, the Regulations for the Payments System comprise Book 01-1. Documents are organized as follows:

General Documentation	Series 01 – 09
External Services Documentation	Series 10 – 49
Internal Services Documentation	Series 50 – 79
Technical Documentation	Series 80 – 99

However, some of the major responsibilities are implicit in the law. For this reason, within the reform project for the LOBCCR and other laws dealing with the financial system, different

suggestions have been included for the modification of several Articles related to the payments system.

7.2 THE RISK CONTROL POLICY

Among the existing measures to avoid the emergence of potential risks, each service has a previously determined clearance cycle that is known by every participant and there are sanctions if such cycles are not complied with. On the other hand, some procedures have been developed for those cases in which an entity is unable to settle. To face such possibilities the participating entities must pledge to the BCCR securities issued by the Treasury or the BCCR itself for all multilateral net clearing services (see Chapter 4).

Participating entities have at their disposal a real-time application (the OLAP tool), which allows them to follow up their collateral position. The OLAP tool also gives them access to other important data for them to manage their payments system activity appropriately.

Although the above-mentioned mechanisms have proven very useful, they might not be sufficient to identify the potential risks that could prevent the continuous and efficient delivery of payment services and in general oversee the adequate operation of the system. For this reason, the BCCR is developing a specific area for the oversight of the payments system, following the recommendations of the Core Principles for Systemically Important Payment Systems of the CPSS of the BIS as well as those of the Western Hemisphere Payments and Securities Clearance and Settlement Initiative.

7.3 SETTLEMENT

According to the LOBCCR every entity subject to the minimum reserve requirement holds a deposit account with the BCCR. With the launch of the clearinghouse and other facilities of the payments system the required reserves plus the exceeding reserves constitute the basic means through which funds are mobilized according to the results of the clearance session. Reserve accounts are mandatory for all institutions participating in the SINPE.

The different services processed through the SINPE have different clearance and settlement cycles: payment messages sent through electronic funds transfers system (TEF) are settled in real time; messages sent using the tax information and settlement services (ILI) are settled in T; the clearance results of the cheque clearing house (CLC), direct credit (CCD) and direct debit (CDD) systems are settled in T + 1.

The BCCR acts as the clearing and settlement agent. In other types of operations the BCCR only executes the settlement, as in the case of the cash-leg for stock market transactions, the money market (MIB), the foreign exchange market (MONED) and the settlement of external services (LSE).

7.4 MONETARY POLICY AND PAYMENT SYSTEMS

The LOBCCR determines the targets and the functions that the BCCR must comply with in reference to monetary policy. Article 2 details the overall objectives of the BCCR in this regard, indicating that

it must ensure that prices fluctuations originated in the monetary and credit markets do not occur or that they be minimized.

Article 3 states that the BCCR has to maintain the external value and convertibility of the domestic currency, define and handle the monetary and foreign exchange policy, issue bills and coins according to the economy real needs, as well as custody of the legal reserves of the financial intermediaries.

The BCCR may use both direct and indirect monetary policy instruments, according to the LOBCCR in the chapter "Monetary, Financial and Foreign Exchange Policy", as well as by the Regulations for Monetary Policy of 1996.

Monetary policy instruments may be classified as follows:

Credit Facilities: The BCCR may execute different credit operations with the financial entities subject to SUGEF supervision in order to protect the stability of the National Financial System. The generic instrument is the discount window, although financial entities may also request emergency loans. In both cases, the Board of Directors of the BCCR is in charge of establishing the limits, authorizing the corresponding transactions and drafting all relevant rules and regulations.

The BCCR may also buy, sell and hold first class securities for investment purposes. These transactions are known as open market transactions. It can also buy Treasury bills, execute operations with international banking and monetary institutions on behalf of the government and trade securities in the banking and stock markets through repos or other similar instruments.

Deposits and Other Liabilities: Beside the legal reserve requirement, the BCCR may also take sight or term deposits, both in domestic or foreign currency.

The OMAs become liabilities when the BCCR attracts resources by issuing its own securities, Monetary Stabilization Bonds (*Bonos de Estabilización Monetaria*, BEMs) or Short Term Investments. In these cases the function of the OMAs is basically associated with the control and stabilization of monetary aggregates. With this same objective the BCCR can also participate in the secondary market of securities buying or selling first class (highly liquid and low credit risk) financial instruments.

Foreign Exchange Policy Instruments: The instruments the Board of Directors of the BCCR has at its disposal to perform the monetary and foreign exchange policies are the following:

- Determining the foreign exchange scheme.
- Authorizing and establishing the requirements for foreign exchange dealing.
- Buying and selling foreign exchange on its own behalf (participation in the MONED system).
- Establishing limits to the proprietary positions that institutions subject to supervision may hold in foreign currency.

- Handling the foreign exchange transactions of the non-banking public sector.
- Carrying out foreign currency forward transactions.

Temporary Instruments: all the above-mentioned instruments may be used at the discretion of the BCCR. However, there are others that can be used only when the economy is significantly unstable, as determined by the Board of Directors of the BCCR. Such instruments are of temporary nature and if adopted, the Legislative Assembly needs to be informed of the reasons for their use and the expected results. In case the Board of Directors decides to extend the use of these instruments beyond the original plans it will need the authorization, through a special law, of both the Executive and Legislative Power. These instruments are:

- Taxes over imported goods.
- Limits to the growth of credit and investment portfolios of the institutions under SUGEF supervision.
- Increases in the reserve requirement. The Board of Directors may increase the reserve requirement above 15 percent and to a maximum of 25 percent for a period no longer than six months.
- The Board of Directors could also establish a maximum range for spreads (financial margin) as well as caps for the fees and other surcharges that financial institutions may charge in credit transactions. In both cases the restriction cannot extend for more than one year.
- Establishment of different foreign exchange regimes and sales of foreign currency. These measures may not last more than one year.

Currently, the direct relationship between Monetary Policy and Payments System actions is limited to the control over the minimum reserve requirements and granting credit facilities. When a participant lacks the necessary funds for settlement in any of the SINPE services, as a last resort solution it may ask the BCCR for a loan. These loans may not exceed 80 percent of the negotiable value of the securities pledged in favor of the BCCR by the corresponding institutions, the interest rate is fixed by the Board of Directors of the BCCR and maturity may not extend beyond seven days, during which the securities must remain immobilized at the CEVAL.

7.5 SECURITIES ISSUES

As mentioned in Chapter 5, the BCCR participates as issuer in both the Joint BCCR-MH auction and the non-auction placement facilities. Through these facilities the BCCR issues the Monetary Stabilization Bonds (BEMs), denominated either in colones or in USD. These bonds are issued for monetary purposes.

7.6 THE ROLE OF THE CENTRAL BANK IN CROSS-BORDER PAYMENTS

In its role as cashier of the State, the BCCR handles the transactions that the Government and other public institutions perform with institutions in foreign countries. However, according to Article 12 of the Regulations for Foreign Exchange Transactions, when dealing with non-banking public institutions the BCCR delegates this task to the State-owned commercial banks. These banks must transfer to non-banking public institutions the foreign exchange currency that was purchased to the BCCR or request the payment of the foreign exchange currency sold to the BCCR no later than the following working day. In these cases the commercial banks are the ones that actually move the funds to/from abroad through their correspondent banks and, more frequently, through SWIFT.

As for the Central Government agencies, through the MH the BCCR receives a TEF authorizing the funds transfer on the Government reserve account in colones or USD. The BCCR then transfers the relevant amounts through SWIFT (since mid-2001) and the corresponding correspondent bank. The most common and important payments in this regard are those associated with the service of external debt and the import of oil-related products.

7.7 PRICING POLICIES

Some of the most relevant features of the pricing policies for the SINPE are the following:

- The destination client of a credit or debit transaction is not charged for received transactions. Thus, the employee receiving his/her salary, the company receiving a payment for the provided goods or services or the client receiving an automatic charge for items such as electricity, water or telephone bill, won't be charged for these transactions.
- Fees are set on a transaction volume basis rather than on transaction value. Since from the standpoint of the IT the operational cost of one transaction worth ₡1.0 is identical to another worth ₡100.0 million or more, the BCCR recognizes that income generation through the SINPE should be based on increasing the actual traffic that goes through the system.
- Fees are defined in USD so that they will not be affected by the devaluation of the domestic currency. Moreover, this has the additional benefit of allowing international comparisons. However, fees must be paid in domestic currency.

This model is based on the existence of different kinds of fees depending on the nature of the participation in the system of every involved part. Thereby, the following fees were defined:

Originating Entity Fee

This corresponds to the charge made by the financial entity (originating entity) to the client (originating client) for each transaction processed through the system. This is merely the payment for the requested credit or debit service. These tariffs are set through private relationships (client/bank).

Operator Fee

This corresponds to the charge made by the system operator (i.e., the BCCR) to the originating entity, for each operation entered into the system using the SINPE platform.

The operator's fees are established in the Regulations for the Payments System and are approved by the BCCR Board of Directors. The BCCR has established a fixed fee for subscription to each of the different services of the SINPE, a charge for every workstation connected to the SINPE, and a variable fee depending on the volume of transactions each entity includes in the system.

These fees aim at recovering the expenses and investments made by the BCCR to make the SINPE operational. However, once these costs are recovered and the system achieves the expected traffic, fees will be reduced to reach a break-even point. The BCCR believes that once economies of scale are achieved, system fees should cover the maintenance and operational expenses of the SINPE.

Destination Entity Fee

This corresponds to the charge made by the destination entity to the originating entity for each received debit or credit transaction, based on the fact that the origin entity uses the destination entity's infrastructure to provide a service to its client.

The destination entity will receive a payment for each received transaction to credit or debit the chequing or savings accounts of its clients.

These fees are determined jointly by the participating entities, using for this purpose the Advisory Commission for the Payments System. The participating entities must honor the fees. Any changes will have to pass through a consultation and approval process within this Commission. Table 12 summarizes the pricing policies of the SINPE.

7.7.1 Collection Procedures

Amounts to be paid are calculated by the BCCR based on the data provided by the SINPE. The BCCR uses a clearing mechanism and charges the reserve accounts of the respective participants.

The amount is calculated in USD and then converted to the domestic currency, using the reference exchange rate of the same day in which the charge is made. Reserve accounts are charged the first working day of the month following the utilization of the service.

7.7.2 Fee Review

Every six months the pricing system is subject to revision and modification by the Advisory Commission of the Payments System. Representatives can make a decision on behalf of the sector they represent.

Table 12: Payments System Pricing Policies
(cost per transaction, in USD)

<i>SERVICE</i>	<i>Origin Entity</i>	<i>BCCR (Operator)</i>	<i>Destination Entity</i>
Cheques Clearing House (CLC)			
Monthly Subscription	To be agreed with the client	300.0	Undefined
Sent Transaction		0.03 each	
Funds Electronic Transfer (TI/TT)			
Monthly Subscription	Same	200.0	5.00 each
Sent Transaction		1.00 each	
Direct Debits (CDD)			
Monthly Subscription	Same	150.0	0.40 each
Sent Transaction		0.01 each	
Direct Credits (CCD)			
Monthly Subscription	Same	150.0	0.60 each
Sent Transaction		0.01 each	
ILI^(a)			
Monthly Subscription	Not applicable	10,000.0	Not applicable

Source: BCCR.

^(a) It is charged only to the Ministry of Finance for being a service created to pay to the Government the taxes collected by the financial entities.

7.7.3 Pricing as a Strategic Element

The BCCR has been using the pricing system as a mechanism to either give incentives or demotivate the use of a determined payment procedure or of a payment instrument versus another. In this regard, it defined a pricing scheme in which prices for payment procedures that are based on sending paper notes or faxes are higher than those for electronic services. By the end of 2001 manual procedures were totally eliminated.

Among the various electronic services, differentiated fees have been established to motivate a more intensive use of a particular payment instrument. For example, fees for cheques are substantially higher than those for direct credits. Also, higher fees were defined for real time services versus deferred batch services.

8 SUPERVISION OF SECURITIES CLEARANCE AND SETTLEMENT SYSTEMS

8.1 SECURITIES REGULATOR SUPERVISORY AND STATUTORY RESPONSIBILITIES

The SUGEF, the SUGEVAL and the SUPEN work under the direction of the CONASSIF. The CONASSIF is responsible for issuing all regulations related to the financial system as well as the general policies for the operation of these three superintendencies. Article 171 of the SML states that the CONASSIF is responsible for dictating the appropriate rules for the authorization, regulation, supervision, control and monitoring that, conforming to the law, the superintendencies must execute.

Thus, CONASSIF is responsible for issuing the general rules for the securities market while the SUGEVAL is responsible for their enforcement as well as for the issuance of specific regulations, which, however, must be approved by the CONASSIF.

The SUGEVAL is the entity responsible for supervising the brokers-dealers, the investment funds managing firms, financial groups, the securities issuers, either financial or not, and the risk rating agencies. The functions of the SUGEVAL are established in Article 3 of the SML, which states that the Superintendency will watch over the transparency of the securities markets, the correct price formation, investor protection and the disclosure of the necessary information. The Superintendency will regulate, supervise and control the securities markets, the activities of all persons and firms who participate either directly or indirectly in these and the acts or contracts related to them.

The main supervisory activities entrusted to the SUGEVAL by the SML are:¹¹⁴

- a. Apply the precautionary measures and sanctions dictated by the law, except those to be imposed by the CONASSIF.
- b. Execute the regulations and other agreements of the CONASSIF.
- c. Approve the bylaws and internal regulations of stock exchanges, clearance and settlement firms, central securities depositories and risk rating agencies.
- d. Authorize equity increases/decrease of stock exchanges, central securities depositories, investment funds managing firms, clearance and settlement firms and of all other persons subject to its control, except for the entities controlled by the SUGEF, issuers and brokers-dealers.
- e. Authorize the functioning of the controlled entities and public offers of securities, and inform CONASSIF on such events.

¹¹⁴ Article 8 of the SML.

- f. Demand from the controlled subjects information on the shares of their corresponding shareholders, board members and employees, including the identification of the end beneficiaries of such holdings. The SUGEVAL may disclose this information to the general public.
- g. Ensure that the controlled entities provide the necessary information to investors.
- h. Demand from the controlled subjects information on the shares of their corresponding shareholders, board members and employees, including the identification of the end beneficiaries of such holdings. The SUGEVAL may disclose this information to the general public.
- i. Provide the public with the maximum possible information about the controlled entities and the situation of the securities market.
- j. Watch over the free competition in the securities market and report the occurrence of monopolistic practices, if any, to the anti-trust authority (*Comisión de Promoción de la Competencia*).
- k. Request the CONASSIF for the suspension, intervention, revoke of license, etc. of the controlled entities and suspend or revoke the authorization for the public offering of securities.
- l. Adopt all the necessary actions for the effective execution of the authorization, regulation, supervision and control functions.

In order to properly comply with its securities market supervisory functions, the SUGEVAL may carry out on site inspections of the controlled entities. Also, the SUGEVAL may inspect market issuers in order to clarify audit information.

Finally, the SUGEVAL is in charge of the organization, regulation and functioning of the National Registry of Securities and Intermediaries (RNV). The latter includes determining the type of information deemed necessary for the RNV and its updating, and regulating the organization and functioning of the registry, identification systems and control of the securities represented by book entries, including the relationships and communications of the entities in charge of such registries with the issuers and the stock exchanges.

8.1.1 Responsibilities Over the Stock Exchanges

Stock exchanges require prior authorization by the SUGEVAL. Similarly, the secondary markets, to be organized by the stock exchanges need prior authorization from the SUGEVAL as well. These authorizations include the approval of the bylaws, regulations, and procedures, including codes of conduct to be mandatory observed by stock exchange personnel, brokers-dealers and their agents. Equity increases and decreases also need the approval of the SUGEVAL.

Stock exchanges must draft and deliver a monthly report to the SUGEVAL on the integration of their investment portfolios.

In more general terms, the SUGEVAL's responsibility over stock exchanges consists of verifying that the corresponding rules are fulfilled, controlling their financial condition, assessing their trading system management, confirming that they have provided all necessary information to the market and that they are carrying out their self-regulatory responsibilities.

The stock exchanges can perform clearance and settlement activities, for which they must comply with the requirements applicable to clearance and settlement firms. Such requirements are described in detail in Section 8.1.3 below.

8.1.2 Responsibilities Over the Central Securities Depositories

Article 134 of the SML states that the securities custody service can only be performed by companies known as Central Securities Depositories, as well as brokers-dealers and the entities subject to the control of the SUGEF. The SUGEVAL is in charge of approving, supervising and dictating the prudential norms for these entities regarding their securities custody activities.¹¹⁵

Thus, central securities depositories must be previously authorized by the SUGEVAL who will approve their constitution, their bylaws and internal regulations before they start operating, as well as subsequent modifications to those documents and the subscription and transmission of equity.

Central securities depositories must comply also with the following:¹¹⁶

- a. They must have a minimum capital according to SUGEVAL's regulations.
- b. When providing the services, they must not discriminate among the users of the National Book Entry System.
- c. They must guarantee the confidentiality of the identity of the securities owners, in accordance with the regulations of the SUGEVAL.
- d. They must keep the profitability of their equity in order to comply with the amounts and capital requirements established by the SUGEVAL. They must also recover from their clients the cost of the services being provided.

CSDs that comply with the requirements established for clearance and settlement firms may also become clearance and settlement agents with the prior authorization of the SUGEVAL.

8.1.3 Responsibility Over Clearance and Settlement Agents

According to the Article 126 of the SML, settlement of the transactions performed through the organized securities markets must be executed through the securities clearance and settlement

¹¹⁵ The SUGEVAL will have to establish necessary mechanisms of coordination if the entities are subject to SUGEF control.

¹¹⁶ Article 119 of the SML.

system ("the system"), integrated by the stock exchanges and the clearance and settlement firms. Brokers-dealers, banks and public institutions complying with the special requirements that the SUGEVAL will determine for this purpose may become settlement agents and shareholders of these companies.

The clearance and settlement companies must comply with the following requirements:

- a. They must receive SUGEVAL's authorization. The SUGEVAL authorizes their constitution, bylaws and internal regulations, as well as any modifications thereof and equity subscription and transmission.
- b. They must have a minimum equity according to the regulations of the SUGEVAL. Stock exchanges are allowed to own no less than 30 percent but no more than 50 percent of the equity of these firms. The remaining capital must be distributed among other settlement members and it must be adjusted according to their settlement throughput, conforming to the requirements established by the SUGEVAL by means of regulations.
- c. They must establish the parameters that settlement members will have to comply with, including criteria such as average trading volume, capital levels, available liquid collateral and all other criteria that the SUGEVAL will establish in the regulations.
- d. When providing the services, they must not discriminate those users that are not shareholders of the company.
- e. They must keep the profitability of their equity in order to comply with the amounts and capital requirements established by the SUGEVAL. They must also recover from their clients the cost of the services being provided.
- f. They must comply with all other requirements to be established by the SUGEVAL with the purpose of ensuring the continuity, security and solvency of the system.

8.1.4 Obligations of Information

The securities issuers must provide the public with timely information, according to the terms established in the SUGEVAL's regulations, on the existence of elements, facts or decisions that could influence, in a major way, the price of their securities. When the issuers believe some information should not be publicly disclosed in order to protect somebody's legitimate interests, they must inform the SUGEVAL, which will decide over the matter.

Market participants receiving and executing orders, and/or advising clients regarding securities investments must provide their clients with all the available information relevant for their investment decisions. This information must be clear, correct, accurate, sufficient and relevant, clearly indicating the involved risks. At the same time, market participants must inform their clients about any type of conflict of interests they may have that could jeopardize their objectivity. The SUGEVAL will set the corresponding rules.

Directors, representatives, agents, employees and advisors of the brokers-dealers, of investment funds managing firms and any other operators in the securities market must inform the SUGEVAL about their economic or other sort of links that could give rise to conflicts of interest.

Moreover, the SUGEVAL may order securities issuers, or any other entity related to the securities market, to communicate immediately to the public any fact or information that, in its criteria, could be relevant for investors, and whose disclosure is necessary to ensure market transparency.

8.1.5 Sanction Capacity of the SUGEVAL

The SUGEVAL is empowered to apply sanctions in the Securities Market, not only to those entities subject to its control but also to any other person or firm that breaks the laws and regulations governing this market. The SUGEVAL may impose sanctions such as public warnings, suspension or temporary limitation of the kind or volume or activities that can be performed by an offender, subsequent monetary penalties, or revoking the authorization for operating in the securities market, depending on whether the infraction is considered very serious, serious or mild.

In order to impose the sanctions determined in Chapter III of the SML, the SUGEVAL, or, if applicable, the stock exchanges, must take into account the following assessment criteria:

- a. The seriousness of the infraction.
- b. The potential or the actual damage.
- c. Any signals that the infractions were intentionally carried out.
- d. Payment capacity.
- e. How long the offender continued with this behavior.
- f. Recidivist behavior of the offender.

8.2 SELF-REGULATORY ORGANIZATIONS SUPERVISORY AND STATUTORY RESPONSIBILITY

8.2.1 Stock Exchanges

The stock exchange functions include authorizing, controlling and regulating brokers-dealers and their agents. Among others, the stock exchange functions and powers are the following:¹¹⁷

- a. Authorize the functioning of the brokers-dealers and of their agents, regulate and supervise their operations in the organized securities market and ensure that these comply with the SML, SUGEVAL regulations and the rules determined by the stock exchange.

¹¹⁷ Article 29 of the SML.

- b. Determine the rules for the functioning of the market they have organized.
- c. Monitor the correct and transparent price formation in the market, and the application of the rules and regulations in the stock exchange negotiations.
- d. Collaborate with the SUGEVAL in its supervisory functions. Stock exchanges should inform the SUGEVAL immediately when they know of any violation to its regulations or to the SML.
- e. Ensure that the brokers-dealers demand the minimum guarantees from their clients, their fulfillment and the appropriate functioning of margins in credit and forward transactions, in accordance with the respective stock exchange regulations.
- f. Suspend, on their own or complying with a decision of the SUGEVAL, the negotiation of securities when inappropriate or disorderly market conditions arise or when transactions non-conforming to the market's best practices are being performed.
- g. Authorize stock exchange agents.
- h. Make available to the public updated information on the securities accepted for trading, issuers and their rating, if any, volume, price, brokers-dealers participating in stocks operations, lists of authorized rating companies, as well as the financial situation of the brokers-dealers and the stock exchange itself, according to SUGEVAL regulations.
- i. Exercise the coercive execution or the contract resolution of stock exchange transactions. In such cases, they must execute the settlement of the cash leg of these transactions and take over the collateral pledged by brokers.¹¹⁸

Regarding the brokers-dealers and their agents the stock exchanges can impose the sanctions described in the Headline IX of the SML. When a stock exchange starts a sanction procedure, this must be communicated immediately to the SUGEVAL. This capacity of the stock exchanges does not preclude the SUGEVAL from starting its own investigations or imposing its own sanctions to the brokers-dealers and their agents.¹¹⁹

8.2.2 Central Securities Depositories

As previously mentioned, the SUGEVAL approves, supervises and determines the prudential regulations for the entities that can provide the securities custody service.

When a central securities depository also acts as a clearance and settlement firm, it must establish the parameters that settlement members must comply with, including criteria such as average trading

¹¹⁸ The provisions relative to the financial settlement will be applicable while the respective stock exchange executes functions of clearance and settlement in accordance with the SML.

¹¹⁹ Article 165 of the SML.

volume, capital levels, available liquid collateral and all other conditions that the SUGEVAL establishes in the regulations.

CEVAL, the only institution that currently provides clearance and settlement services for securities trades, has established in its internal regulations that all transactions will be regulated, controlled and monitored by its Board of Directors or by the entity appointed by the CEVAL for this purpose.

8.3 CAPACITY AND SAFEGUARD OF THE SYSTEM

In the actual custody, clearance and settlement systems attention is paid to the operational reliability of the different systems. Every year a contingency committee inside the BNV performs an analysis of the potential threats and the existing contingency plan is adapted to the results of this analysis.

Communication between BNV and the brokers-dealers is based on an infrastructure client-server. Each participant is connected to the server through two dedicated optic fiber lines. The capacity of the system allows it to handle up to twice the number of transactions currently being processed at peak-hours. An external expert periodically tests protection measures against the non-authorized access to the stock exchange systems.

The BNV has its own power supply, which enables it to cope with any electricity blackout. On the other hand, a back-up server does not exist in hot standby mode and there is no alternative site for contingencies.

With reference to the development of computer systems, the BNV elaborated procedures for the development and modification of the systems. Any changes are subject to numerous tests before they actually become operational. Systems have separated environments for production, development and testing. A "Modifications Committee" was created and includes participants from the information technology department, those who actually designed and implemented the modifications, from the internal audit department and the person in charge of running the corresponding tests for modifications. The BNV's President chairs this Committee.

APPENDIX: STATISTICAL TABLES

The first series of tables (A) are statistics on payments and securities clearance and settlement in Costa Rica. The second series (B) are more general statistic related to the financial sector.

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Table A1: Basic Statistical Data

	1996	1997	1998	1999	2000 ^(a)	2001 ^(a)
Population, in thousands ^(b)	3,593.1	3,681.2	3,768.9	3,856.2	3,943.2	4,030.0
GDP (USD million)	11,843.2	12,829.0	14,095.9	15,796.6	15,948.2	16,362.5
GDP <i>per capita</i> (in USD)	3,296.1	3,485.0	3,740.1	4,096.4	4,044.5	4,060.2
Exchange Rate colones/USD ^(b)	207.7	232.6	257.2	285.7	308.2	328.9

Sources: BCCR and Universidad de Costa Rica.

^(a) Preliminary Data.

^(b) As of June 30 for all the years.

^(c) Bid-ask annual average.

Table A2: Settlement Media Used by Non-Banks

(in millions of colones, end of year)

	1996	1997	1998	1999	2000	2001
Notes and Coins issues	115,766	146,844	165,349	229,813	202,711	223,035
<i>In the hands of the public</i>	91,743	106,815	124,167	144,264	143,027	158,090
Current Account Deposits, domestic currency	104,933	174,873	192,144	237,312	300,454	328,495
Current Account Deposits, foreign currency	269,907	331,012	462,582	564,190	697,144	819,794
Narrow Money Supply (M1)	196,676	281,688	316,310	381,577	443,481	486,585
Domestic Currency Liquidity (M2)	535,424	617,172	727,260	846,835	1,016,231	1,058,555
Broad Monetary Aggregate (M3)	805,332	948,184	1,189,841	1,411,024	1,713,375	1,878,341

Source: BCCR.

Table A3: Settlement Media Used by Credit/Deposit Taking Institutions

(in millions of colones, end of year)

	1996	1997	1998	1999 ^(a)	2000	2001
Domestic currency						
<i>Required reserves held at the BCCR</i>	60,874	67,923	77,944	95,588	90,582	54,302
<i>Excess reserves held at the BCCR</i>	5,178	4,532	5,720	-20,928	6,249	7,009
Foreign currency (USD)						
<i>Required reserves held at the BCCR</i>	115	113	99	93	102	124
<i>Excess reserves held at the BCCR</i>	7	14	7	-2	3	0

Source: BCCR.

^(a) Figures for 1999 reflect the precautionary measures taken by the Board of Directors of the BCCR regarding the potential withdrawals of funds associated with Y2K fears.

Table A4: Institutional Framework
(as of December, 2001)

	<i>Number of institutions</i>	<i>Number of branches^(a)</i>	<i>Number of accounts</i>	<i>Value of accounts^(b) (in ¢ billion)</i>
Central Bank	1	-	-	-
Commercial Banks	21	384	N.A.	1.665
<i>State-owned Banks</i>	3	218	N.A.	1.104
<i>Private Banks</i>	16	128	N.A.	418
<i>Banks created by Special Laws</i>	2	38	N.A.	143
Non-Banking Financial Firms	12	12	N.A.	21
Savings and Loans Cooperatives	25	36	N.A.	41
Entities related to the National Housing System	3	44	N.A.	90
Other Financial Institutions	1	0	N.A.	2

Sources: BCCR and SUGEF.

^(a) Includes branches, representative offices and agencies.

^(b) Represents the aggregated value of deposit accounts, current accounts and term accounts of the entities controlled by the SUGEF.

Table A5: Bank Notes and Coins
(in millions of colones, end of year)

	1996	1997	1998	1999	2000	2001
Notes and Coins Issued	115,766	146,844	165,349	229,813	202,711	223,035
Notes:						
10,000	N.A.	N.A.	8,234	81,420	88,533	110,922
5,000	83,917	113,653	120,544	105,590	70,824	65,587
2,000	N.A.	N.A.	1,042	6,564	7,732	8,752
1,000	20,178	18,491	19,607	18,655	17,264	17,973
500	3,542	5,087	4,713	4,768	4,881	4,553
100	3,547	2,648	2,129	1,009	596	559
50	1,054	1,397	1,357	1,072	584	473
20	29	29	29	29	29	29
10	40	39	40	40	40	40
5	82	80	82	82	82	82
Coins	3,377	5,420	7,572	10,585	12,146	14,065
Notes and Coins Held by Credit Institutions	24,022	40,029	41,183	85,549	59,684	64,945
Notes and Coins in Circulation	91,743	106,815	124,167	144,264	143,027	158,090

Source: BCCR.

Table A6: Cash Dispensers, ATMs and EFTPOS Terminals^(a)
(end of year)

	1996	1997	1998	1999	2000	2001
ATMs						
Number of Terminals	68	178	263	328	470	514
Volume of Transactions	1,771,474	6,365,761	6,334,396	20,352,111	34,465,512	50,003,123
Value of Transactions (in millions of colones)	23,071	42,394	147,420	289,548	743,229	757,208
Cash Dispensers						
Number of Terminals	N.A.	7	31	35	67	57
Volume of Transactions	N.A.	365,942	536,543	485,373	1,198,116	603,841
Value of Transactions (in millions of colones)	N.A.	3	7,175	9,333	20,508	8,357
EFTPOS Terminals ^(b)	N.A.	1,986	4,166	4,424	7,553	9,436

Sources: Commercial Banks and ATM Network Managing Firms.

^(a) This information was not available for all entities in all the years. Information of entities that shut down or merged in year 2001 was not available either. Thus, figures in this table must be considered only as proxies.

^(b) Represents debit and credit card electronic paying devices and electronic purses.

Table A7: Number of Payment Cards in Circulation^(a)
(end of year)

	1996	1997	1998	1999	2000	2001
Cards with a Debit/Credit function						
Debit Cards	69,543	139,468	241,795	935,410	937,679	1,327,907
Credit Cards	57,961	66,022	115,563	160,147	177,970	198,915
Others ^(b)	0.	0	34,394	60,374	114,425	104,380

Source: Commercial Banks and Card Issuers.

^(a) This information was not available for all entities in all the years. Information of entities that shut down or merged in year 2001 was not available either. Thus, figures in this table must be considered only as proxies.

^(b) Represents prepaid cards and electronic purses.

Table A8: Indicators of Use of Various Cashless Payment Instruments^(a)
(volume of transactions)

	1996	1997	1998	1999	2000	2001
Cheques issued ^(b)						
In domestic currency	13,780,662	13,421,653	14,022,598	14,315,566	21,688,980	21,401,349
In foreign currency	211,370	254,751	305,693	493,330	646,317	700,667
Payments with Cards						
Debit	462,649	1,116,895	2,149,688	6,244,627	9,178,188	11,496,396
Credit	1,298,382	1,507,736	3,961,057	4,985,646	6,085,756	6,117,673
Paper-based Credit Transfers ^(c)	15,815	63,260	79,075	93,329	142,430	208,985
Paperless Credit Transfers ^(b)	93,640	105,560	141,390	231,587	376,542	3,763,239
Automatic debits	34,540	44,151	270,647	375,921	501,330	577,550

Sources: Commercial Banks and Card Issuers.

^(a) This information was not available for all entities in all the years. Information of entities that shut down or merged in year 2001 was not available either. Thus, figures in this table must be considered only as proxies.

^(b) Represents transactions not processed through the SINPE.

^(c) Represents paper-based transactions within the banks themselves.

Table A9: Indicators of Use of Various Cashless Payment Instruments^(a)
(value of transactions, in colones million)

	1996	1997	1998	1999	2000	2001
Cheques issued ^(b)						
In domestic currency	3,544,780	4,370,101	5,289,948	6,725,073	8,286,397	7,047,306
In foreign currency	3,053	3,874	4,965	9,310	10,508	5,193
Payments with Cards						
Debit	2,630	7,424	20,934	45,154	75,663	105,699
Credit	15,711	19,970	60,561	90,792	111,858	137,577
Paper-based Credit Transfers ^(c)	18	32	46	2,258	2,610	2,786
Paperless Credit Transfers ^(b)	331,041	354,867	848,216	2,465,822	3,497,418	3,913,390
Automatic debits	368	517	4,772	7,762	9,839	12,120

Sources: Commercial Banks and Card Issuers.

^(a) This information was not available for all entities in all the years. Information of entities that shut down or merged in year 2001 was not available either. Thus, figures in this table must be considered only as proxies.

^(b) Represents transactions not processed through the SINPE.

^(c) Represents paper-based transactions within the banks themselves.

**Table A10: Payment Instructions Handled by Selected
Interbank Transfers Systems**
(volume of transactions, in thousands)

	1997	1998	1999	2000	2001
Cheque Clearinghouse (CLC)	8,485.3	12,496.1	12,977.3	12,321.8	11,601.0
<i>In Domestic Currency</i>	8,324.3	12,225.1	12,629.4	11,904.1	11,101.6
<i>In Foreign Currency</i>	161.1	271.0	347.9	417.7	499.4
Electronic Funds Transfers	N.A.	N.A.	17.6	46.8	71.2
<i>Interbank (TI)</i>	-	-	17.6	43.6	39.8
<i>In Domestic Currency</i>	-	-	14.1	32.9	30.9
<i>In Foreign Currency</i>	-	-	3.5	10.7	8.9
<i>Among third parties (TT)</i>	-	-	-	3.2	31.4
<i>In Domestic Currency</i>	-	-	-	2.8	22.7
<i>In Foreign Currency</i>	-	-	-	0.4	8.7
Tax Information and Settlement (ILI)	N.A.	N.A.	N.A.	N.A.	5.2
<i>In Domestic Currency</i>	-	-	-	-	4.8
<i>In Foreign Currency</i>	-	-	-	-	0.4
Direct Credits (CD)	N.A.	N.A.	N.A.	N.A.	2,426.7
<i>In Domestic Currency</i>	-	-	-	-	2,426.6
<i>In Foreign Currency</i>	-	-	-	-	0.057
Direct Debits (CDD)	N.A.	N.A.	N.A.	N.A.	0.034
<i>In Domestic Currency</i>	-	-	-	-	0.034
<i>In Foreign Currency</i>	-	-	-	-	0
MIB	104	2,808	1,612	5,391	12,088
<i>In Domestic Currency</i>	54	2,178	932	4,181	9,034
<i>In Foreign Currency</i>	50	630	680	1,210	3,054
MONED	N.A.	4,112	33,084	35,234	29,020

Source: BCCR.

Note: The systems in which a "N.A." has been inserted were not operational as of these dates.

Table A11: Payment Instructions Handled by Selected Interbank Transfers Systems

(value of transactions, in millions of colones and of USD)

	1997	1998	1999	2000	2001
Cheque Clearinghouse (CLC)	8,048,423	11,890,819	11,823,086	9,795,096	8,367,937
<i>In Domestic Currency</i>	6,958,825	9,664,136	8,906,886	7,528,679	6,616,604
<i>In Foreign Currency</i>	4,680	8,650	10,199	7,348	5,321
Electronic Funds Transfers	N.A.	N.A.	2,963,624	6,007,331	9,064,683
<i>Interbank (TI)</i>	-	-	2,963,624	5,776,160	7,009,717
<i>In Domestic Currency</i>	-	-	1,767,579	3,622,632	4,200,963
<i>In Foreign Currency</i>	-	-	4,183	6,982	8,533
<i>Among third parties (TT)</i>	-	-	-	231,171	2,054,967
<i>In Domestic Currency</i>	-	-	-	187,373	1,369,797
<i>In Foreign Currency</i>	-	-	-	142	2,082
Tax Information and Settlement (ILI)	N.A.	N.A.	N.A.	N.A.	446,564
<i>In Domestic Currency</i>	-	-	-	-	444,836
<i>In Foreign Currency</i>	-	-	-	-	5
Direct Credits (CCD)	N.A.	N.A.	N.A.	N.A.	224,031
<i>In Domestic Currency</i>	-	-	-	-	220,919
<i>In Foreign Currency</i>	-	-	-	-	9
Direct Debits (CDD)	N.A.	N.A.	N.A.	N.A.	147
<i>In Domestic Currency</i>	-	-	-	-	147
<i>In Foreign Currency</i>	-	-	-	-	0
MIB	8,084	420,491	475,907	1,885,832	4,053,164
<i>In Domestic Currency</i>	4,918	346,354	380,406	1,727,294	3,356,003
<i>In Foreign Currency</i>	14	288	334	514	2,118
MONED	N.A.	214,003	1,667,770	2,098,677	2,580,993
Memo Item: Exchange rate ^(a)	232.82	257.42	285.93	308.44	329.16

Source: BCCR.

^(a) Bid-ask annual average.

Note: The systems in which a "N.A." has been inserted were not operational as of these dates.

Table A12: Securities and Accounts Registered in the Central Securities Depository

	1997	1998	1999	2000	2001
Number of Securities Registered ^(a)	62,221	70,009	71,794	73,812	79,496
Number of Accounts	47	49	81	73	71

Source: CEVAL.

^(a) Includes global notes, physical certificates and shares.**Table A13: Securities Holdings in the Central Securities Depository**
(in millions of colones and of USD)

	1997	1998	1999	2000	2001
Securities Holdings in the CEVAL	409,855	588,331	1,060,821	1,362,047	1,673,878
<i>In colones</i>	267,903	446,369	763,561	911,610	1,067,062
<i>In USD</i>	610	552	1,040	1,460	1,844

Source: CEVAL.

Table A14: Transfer Instructions Handled by the CEVAL
(volume of transactions)

	1997	1998	1999	2000	2001
Government Securities	70,484	403,796	440,269	347,498	436,792
Corporate Bonds	64,464	187,954	200,934	122,331	109,651
Equities	5,142	15,364	28,052	22,560	27,060
Others	7,606	17,428	22,866	64,924	53,243

Source: CEVAL.

Table A15: Transfer Instructions Handled by the CEVAL
(value of transactions, in millions of colones)

	1997	1998	1999	2000	2001
Government Securities	485,209	3,392,216	6,226,211	7,892,703	22,487,791
Corporate Bonds	290,983	1,319,066	1,948,226	1,287,996	4,357,673
Equities	7,192	13,723	44,658	42,549	7,167
Others	37,350	169,538	333,816	733,485	857,411

Source: CEVAL.

Table A16: Participation in SWIFT by Domestic Institutions

	1996	1997	1998	1999	2000	2001
Domestic SWIFT Users	-	1	3	7	10	11
<i>Members</i>	-	-	-	-	1	1
<i>Sub-members</i>	-	-	1	1	2	2
<i>Participants</i>	-	1	2	6	7	8
SWIFT Users Worldwide	5,632	6,176	6,557	6,797	7,125	7,199
<i>Members</i>	2,874	2,985	2,980	2,214	2,288	2,241
<i>Sub-members</i>	2,404	2,585	2,720	2,763	2,978	3,027
<i>Participants</i>	354	606	857	1,820	1,859	1,931

Source: SWIFT.

Table A17: SWIFT Message Flows To / From Domestic Users

	1996	1997	1998	1999	2000	2001
Total Messages Sent						
<i>Of which</i>						
<i>Category I</i>	N.A.	N.A.	—	—	65,825	124.234
<i>Category II</i>	N.A.	N.A.	—	—	8,531	14.715
Total Messages Sent						
<i>Category I</i>	N.A.	N.A.	—	—	68,232	122.417
<i>Category II</i>	N.A.	N.A.	—	—	2,044	3.447
Global SWIFT Traffic	679,571,032	795,971,982	907,617,576	1,015,105,357	1,223,771,421	N.D.

Source: SWIFT.

Table B1: Number of Financial Entities
(end of year)

	1996	1997	1998	1999	2000	2001
Financial System Total						
Banks	28	28	28	26	23	21
State-owned	3	3	3	3	3	3
Created by Special Laws	N.A.	N.A.	2	2	2	2
Private	25	25	23	21	18	16
Non-banking financial firms	18	21	17	15	13	12
Savings and Loans Cooperatives ^(a)	34	40	39	27	26	25
Mutuals ^(b)	N.A.	N.A.	4	4	4	3
Other Financial Institutions	N.A.	N.A.	1	1	1	1
Financial Groups	N.A.	N.A.	N.A.	19	21	21

Source: SUGEF.

^(a) Supervised by the SUGEF.

^(b) Entities comprising the National Housing Financial System.

Table B2: Number of Deposit, Chequing and Savings Accounts
(in thousands, end of year)

	1996	1997	1998	1999	2000	2001 ^(c)
Financial System Total	N.A.	N.A.	N.A.	N.A.	N.A.	N.A.
Banks	N.A.	N.A.	N.A.	N.A.	N.A.	2,333,770
State-owned	N.A.	N.A.	N.A.	N.A.	N.A.	2,026,149
Created by Special Laws	N.A.	N.A.	N.A.	N.A.	N.A.	N.A.
Private	N.A.	N.A.	N.A.	N.A.	N.A.	307,621
Non-banking financial firms	N.A.	N.A.	N.A.	N.A.	N.A.	N.A.
Savings and Loans Cooperatives ^(a)	N.A.	N.A.	N.A.	N.A.	N.A.	N.A.
Mutuals ^(b)	N.A.	N.A.	N.A.	N.A.	N.A.	N.A.
Other Financial Institutions	N.A.	N.A.	N.A.	N.A.	N.A.	N.A.

Source: SUGEF.

^(a) Supervised by the SUGEF.

^(b) Entities comprising the National Housing Financial System.

^(c) Represents the number of clients holding sight deposits as of December 31.

Table B3: Assets
(in billions of colones, end of year)

	1996	1997	1998	1999	2000	2001 ^(c)
Financial System Total	1,062.8	1,062.8	1,286.0	1,644.4	1,918.0	2,789.2
Banks	1,004.9	1,136.3	1,470.1	1,724.4	2,171.2	2,501.6
<i>State-owned</i>	726.4	780.8	960.2	1,098.3	1,289.1	1,370.8
<i>Created by Special Laws</i>	107.7	149.2	173.1	212.6	250.9	299.8
<i>Private</i>	170.8	206.3	336.8	413.4	630.9	831.1
Non-banking financial firms	5.7	8.7	13.0	18.0	26.7	34.0
Savings and Loans Cooperatives ^(a)	32.9	43.4	51.2	55.5	68.4	90.0
Mutuals ^(b)	N.A.	73.8	79.8	81.4	87.1	105.0
Other Financial Institutions	19.3	23.8	30.2	38.7	48.1	58.6

Source: SUGEF.

^(a) Supervised by the SUGEF.

^(b) Entities comprising the National Housing Financial System.

^(c) Preliminary data.

Table B4: Deposits
(in billions of colones, end of year)

	1996	1997	1998	1999	2000	2001 ^(c)
Financial System Total	643.6	811.9	1,113.0	1,332.0	1,649.1	1,819.5
Banks	625.0	801.1	1,043.0	1,254.2	1,527.9	1,665.0
<i>State-owned</i>	495.9	631.5	781.7	929.5	1,078.5	1,103.9
<i>Created by Special Laws</i>	48.8	53.4	64.9	91.8	112.1	143.5
<i>Private</i>	80.2	116.2	196.5	232.9	337.4	417.7
Non-banking financial firms	2.5	5.2	7.5	10.4	16.1	20.9
Savings and Loans Cooperatives ^(a)	15.1	22.5	24.0	25.4	31.4	41.1
Mutuals ^(b)	N.A.	N.A.	63.3	70.0	83.0	90.0
Other Financial Institutions	1.0	1.1	1.5	1.8	2.2	2.5

Source: SUGEF.

^(a) Supervised by the SUGEF.

^(b) Entities comprising the National Housing Financial System.

^(c) Preliminary data.

Table B5: Equity
(in billions of colones, end of year)

	1996	1997	1998	1999	2000	2001 ^(c)
Financial System Total	130.2	166.8	215.0	266.5	322.5	378.4
Banks	100.4	128.2	161.5	200.5	241.5	280.6
<i>State-owned</i>	39.3	53.4	62.4	77.4	95.4	112.1
<i>Created by Special Laws</i>	35.7	45.5	53.0	63.7	74.7	84.6
<i>Private</i>	25.4	29.3	46.2	59.4	71.4	83.9
Non-banking financial firms	1.4	2.6	4.5	5.5	6.5	7.6
Savings and Loans Cooperatives ^(a)	10.4	13.6	16.4	19.1	23.1	27.9
Mutuals ^(b)	N.A.	N.A.	4.1	4.9	5.8	6.5
Other Financial Institutions	17.9	22.4	28.5	36.5	45.6	55.7

Source: SUGEF.

^(a) Supervised by the SUGEF.

^(b) Entities comprising the National Housing Financial System.

^(c) Preliminary data.

Table B6: Loans
(in billions of colones, end of year)

	1996	1997	1998	1999	2000	2001 ^(c)
Financial System Total	374.4	497.3	830.7	993.5	1,258.7	1,555.2
Banks	356.1	470.7	714.0	862.0	1,105.5	1,347.9
<i>State-owned</i>	130.1	177.8	327.1	400.5	504.7	603.7
<i>Created by Special Laws</i>	69.2	85.6	109.7	113.3	127.2	160.8
<i>Private</i>	156.7	207.3	277.2	348.2	473.6	583.4
Non-banking financial firms	5.9	11.6	10.0	12.6	18.7	25.0
Savings and Loans Cooperatives ^(a)	N.A.	N.A.	35.8	37.4	45.8	59.9
Mutuals ^(b)	N.A.	N.A.	52.4	59.2	60.2	77.6
Other Financial Institutions	12.5	15.0	18.5	22.3	28.4	44.7

Source: SUGEF.

^(a) Supervised by the SUGEF.

^(b) Entities comprising the National Housing Financial System.

^(c) Preliminary data.

Table B 7: Equities Market

	1996	1997	1998	1999	2000	2001
Traded Value (in millions of colones)	3,343	6,191	16,328	12,217	19,778	24,079
Traded Value / GDP (%)	0.14	0.21	0.45	0.27	0.40	0.45
Number of Registered Firms	24	17	17	16	16	16

Source: SUGEVAL.

Table B8: Issues in International Capital Markets
(balances in millions of USD)

	Issues	Grace Period	Repayment Period	Coupon	Balance as of December 31, 2001
Total					1,410.4
Central Bank ^(a)					
Principal "A" Bonds	1	10	20 semesters	6.25%	176.7
Principal "B" Bonds	1	15	20 semesters	6.25%	214.1
National Government ^(b)					
Issued 30-04-1998	1	5	01-05-2003	8.00%	200.0
Issued 06-05-1999	1	10	15-05-2009	9.35%	300.0
Issued 27-07-2000	1	20	01-08-2020	9.99%	250.0
Issued 01-03-2001	1	10	01-03-2011	9.00%	250.0
Instituto Costarricense de Electricidad (ICE)					
Issued 03-09-1997	1	0	28 semesters	7.94%	11.8
Issued 03-09-1997	1	0	28 semesters	7.94%	7.9

Source: BCCR.

^(a) These are Brady Bonds that originated from the impossibility to repurchase some amounts of external public debt with the May 1990 Agreement.^(b) Law 7970 of January 10, 2000 authorized the following amounts to be issued in international capital markets: USD 250 million in 2001, USD 250 million in 2002, USD 450 million in 2003, and USD 250 million in 2004.

Table B9: Financial Institutions and Financial Groups Supervised by the SUGEF
(as of December 31, 2001)

I. State-owned Commercial Banks

Banco Crédito Agrícola de Cartago
Banco de Costa Rica
Banco Nacional de Costa Rica

II. Banks Created by Special Laws

Banco Hipotecario de la Vivienda
Banco Popular y de Desarrollo Comunal

III. Private Banks

Banco Promérica S.A.
Banco BanCrecen S.A.
Banco Banex S.A.
Banco Bantec CQ S.A.
Banco BCT S.A.
Banco Cathay de Costa Rica S.A.
Banco Cooperativo Costarricenses R.L. ^(a)
Banco Cuscatlán de Costa Rica S.A.
Banco de Crédito Centroamericano (BANCENTRO) S.A.
Banco de San José S.A. ^(b)
Banco Elca S.A.
Banco Finandesa S.A. ^(b)
Banco Improsa S.A.
Banco Interfin S.A.
Banco Internacional de Costa Rica S.A.
Banco Solidario de Costa Rica S.A. ^(a)
Banco Uno S.A.
Citibank (Costa Rica) S.A.
Scotiabank de Costa Rica S.A.

^(a) Bankruptcy has been solicited to courts.

^(b) Merger in process. Banco de San José S.A. will prevail.

IV. Non-banking Financial Firms

Compañía Financiera de Londres Ltda.
Corporación Financiera C.F. S.A.
Corporación Financiera Miravalles S.A.
Fiduciaria de Ahorro Banex S.A.
Financiera Belén S.A. ^(c)

Financiera Brunca S.A.^(c)
Financiera Cafsa S.A.
Financiera Comeca S.A.
Financiera Desyfin S.A.
Financiera Más X Menos S.A.^(d)
Financiera Multivalores S.A.
Financiera Trisan S.A.
La Unión Financiera Aduanera S.A.

^(c) Merger in process. Financiera Brunca S.A. will prevail.

^(d) The name will change to Financiera Servivalores S.A.

V. Savings and Loans Cooperatives

Cemsucoop R.L.
Coocique R.L.
Coopavegra R.L.
Coope san marcos R.L.
Coopeacosta R.L.
Coopealianza R.L.
Coope-ande No. 1 R.L.
Coopeande No. 7 R.L.
Coopeaserrí R.L.
Coopecaja R.L.
Coopecar R.L.
Coopecorrales R.L.
Coopefyl R.L.
Coopegrecia R.L.
Coopejudicial R.L.
Coopemep R.L.
Coopemex R.L.^(e)
Coopenae R.L.
Coopeorotina R.L.
Coopesanramón R.L.
Coopeservidores R.L.
Coopesparta R.L.
Coopetacares R.L.
Coopmani R.L.
Cootilarán R.L.^(e)
Credecoop R.L.
Servicoop R.L.

^(e) Merger in process. Coopemex R.L. will prevail.

VI. Entities comprising the National Housing Financial System

La Vivienda Mutual de Ahorro y Préstamo

Mutual Alajuela de Ahorro y Préstamo^(f)

Mutual Cartago de Ahorro y Préstamo

Mutual Heredia de Ahorro y Préstamo^(f)

^(f) Merger in process. Mutual Alajuela de Ahorro y Préstamo will prevail.

VII. Other Financial Institutions

Caja de Ahorro y Préstamos de la ANDE

VIII. Foreign Exchange Market Institutions

BN Valores Puesto de Bolsa^(g)

Corporación Bursátil Centroamericana, Puesto de Bolsa S.A.^(g)

Casa de Cambio Ofinter^(h)

Casa de Cambio Vinir S.A.^(h)

Casa de Cambio Tele Dólar Expreso S.A.^{(h)(i)}

Inversiones Sama, Puesto de Bolsa S.A.^(g)

Puesto de Bolsa Interbolsa S.A.^(g)

Serfín Valores Puesto de Bolsa S.A.^(g)

^(g) Only their compliance with foreign exchange regulation is supervised by the SUGEF.

^(h) This can only buy and sell foreign currencies.

⁽ⁱ⁾ Authorized to participate in the foreign exchange market, although not yet operational.

IX. Financial Groups^(j)

Grupo Financiero Acobo

Grupo Financiero Alianza^(k)

Grupo Financiero Bancrecen

Grupo Financiero Banex^(l)

Grupo Financiero Bantec

Grupo Financiero BCT

Grupo Financiero BNS de Costa Rica

Grupo Financiero Cathay

Grupo Financiero Citibank

Grupo Financiero Coocique

Grupo Financiero Cuscatlán

Grupo Financiero Elca

Grupo Financiero Finadesa^(m)

Grupo Financiero Improsa

Grupo Financiero Interfín

Grupo Financiero Lafise

Grupo Financiero Metropolitano^(j)

Grupo Financiero Pacífico

Grupo Financiero Promérica

Grupo Financiero San José^(m)

Grupo Financiero Servivalores

^(j) General information on financial groups is available for the general public at the SUGEF.

^(k) The CONASSIF authorized it as financial group on September 2001.

^(l) Merger in process. Grupo Financiero Banex will prevail.

^(m) Merger in process. Grupo Financiero Banex will prevail.

^(a) Merger in process. Grupo Financiero San José will prevail.

Source: SUGEF.

LIST OF ABBREVIATIONS

ABC	<i>Asociación Bancaria Costarricense</i> (Costa Rican ' Bankers' Association)
AGB	<i>Auditoría General de Bancos</i> (Banks' General Audit)
AGEF	<i>Auditoría General de Entidades Financieras</i> (Financial Sector General Audit)
AID	Agency for International Development
AES	<i>Administración de Esquemas de Seguridad</i> (Management of Security Schemes)
ATM	Automated Teller Machine
BANVHI	<i>Banco Hipotecario de la Vivienda</i> (Housing Mortgage Bank)
BCCR	<i>Banco Central de Costa Rica</i> (Central Bank of Costa Rica)
BEM	<i>Bonos de Estabilización Monetaria</i> (Monetary Stabilization Bonds)
BIS	Bank for International Settlements
BNV	<i>Bolsa Nacional de Valores</i> (National Stock Exchange)
CAT	<i>Certificado de Abono Tributario</i> (Tax Bonus Certificate)
CAV	<i>Cuentas de Administración de Valores</i> (Securities Administration Accounts)
CC	<i>Cuenta Cliente</i> (Customer Account)
CD	<i>Créditos Directos</i> (Direct Credits)
CCD	<i>Servicio de Compensación de Créditos Directos</i> (Direct Credits Clearing Service)
CCSS	<i>Caja Costarricense del Seguro Social</i> (Costa Rica's Social Security Institute)
CDD	<i>Servicio de Compensación de Débitos Directos</i> (Direct Debits Clearing Service)
CEVAL	<i>Central de Valores de la Bolsa Nacional de Valores, S.A.</i> (National Stock Exchange Central Securities Depository)
CICAD	<i>Centro de Inteligencia Conjunto Antidrogas</i> (Joint Anti-narcotics Intelligence Centre)
CLC	<i>Compensación y Liquidación de Cheques y otros Valores</i> (Cheque Clearing and Settlement)
CONASSIF	<i>Consejo Nacional de Supervisión del Sistema Financiero</i> (National Council for the Supervision of the Financial System)
COV	<i>Compensación de Otros Valores</i> (Clearing and Settlement of Other Documents)
CPSS	Committee on Payment and Settlement Systems
CSD	Central Securities Depository
DD	<i>Débitos Directos</i> (Direct Debits)
EFTPOS	Electronic Funds Transfer at the Point of Sale

EML	<i>Encaje Mínimo Legal</i> (Minimum Bank Reserve Requirement)
FDI	Foreign Direct Investment
GDP	Gross Domestic Product
GIC	<i>Sistema de Gestión de Instrucciones</i> (Instruction Management System)
ICAF	<i>Instituto Centroamericano de Finanzas y Mercado</i> (Central American Finance and Market Institute)
ICE	<i>Instituto Costarricense de Electricidad</i> (Costa Rican Institute for Electricity)
ICT	<i>Instituto Costarricense de Turismo</i> (Costa Rican Institute for Tourism)
ILI	<i>Información y Liquidación de Impuestos</i> (Tax Information and Settlement)
IMF	International Monetary Fund
INS	<i>Instituto Nacional de Seguros</i> (National Insurance Institute)
ISIN	International Securities Industry Numbering
ITCER	<i>Índice de Tipo de Cambio Efectivo Real Multilateral</i> (Multilateral Real Exchange Rate Index)
LOBCCR	<i>Ley Orgánica del Banco Central de Costa Rica</i> (Organic Law of the Central Bank of Costa Rica)
LOSBN	<i>Ley Orgánica del Sistema Bancario Nacional</i> (Organic Law of the National Banking System)
LSE	<i>Liquidación de Servicios Externos</i> (Settlement of External Services)
MIB	<i>Mercado Interbancario</i> (Interbank Money Market)
MICR	Magnetic Ink Character Recognition
MH	<i>Ministerio de Hacienda</i> (Ministry of Finance)
MONED	<i>Mercado Organizado para la Negociación Electrónica de Divisas</i> (Organized Market for the Electronic Trading of Currencies)
OLAP	On-line Analytical Processing
OMA	<i>Operaciones de Mercado Abierto</i> (Open Market Transactions)
OPAB	<i>Operaciones de Administración Bursátil</i> (Stock Market Management Transactions)
OPC	<i>Operadora de Planes de Pensiones Complementarias</i> (Complementary Pension Funds Managing Firms)
PAE	<i>Programa de Ajuste Estructural</i> (Structural Adjustment Program)
POS	Point of Sale
PPP	Purchasing Power Parity
PVP	Payment Versus Payment
RECOPE	<i>Refinadora Costarricense de Petróleo</i> (Costa Rican Oil Refinery)

RNVI	<i>Registro Nacional de Valores e Intermediarios</i> (National Registry of Securities and Intermediaries)
ROPV	<i>Reglamento sobre Oferta Pública de Valores</i> (Regulations for the Public Offering of Securities)
RSP	<i>Responsable de Seguridad Parcial</i> (Responsible for Partial Security)
RST	<i>Responsable de Seguridad Total</i> (Responsible for Total Security)
RTGS	Real Time Gross Settlement
SAC	<i>Sistema de Anotación en Cuenta</i> (Book Entry System)
SAFI	<i>Sociedades Administradoras de Fondos de Inversión</i> (Investment Funds Managing Firms)
SAO	<i>Sala Alternativa de Operaciones</i> (Alternate Operations Hall)
SIL	<i>Sistema Interbancario de Liquidación</i> (Interbank Settlement System)
SINPE	<i>Sistema Interbancario de Negociación y Pagos Electrónicos</i> (Electronic Interbank Trading and Payment System)
SML	Securities Market Law
STP	Straight Through Processing
SUGEf	<i>Superintendencia General de Entidades Financieras</i> (General Superintendency of Financial Entities)
SUGEVAL	<i>Superintendencia General de Valores</i> (General Superintendency of Securities)
SUPEN	<i>Superintendencia de Pensiones</i> (Superintendency of Pensions)
SWIFT	Society for Worldwide Interbank Financial Telecommunications
TEF	<i>Transferencia Electrónica de Fondos</i> (Electronic Funds Transfer)
TEF 3	<i>Transferencia Electrónica de Fondos entre Terceros</i> (Third Party Electronic Funds Transfer)
TI	<i>Transferencia Interbancaria</i> (Interbank Funds Transfer)
TT	<i>Transferencia de Terceros</i> (Third Party Funds Transfer)
UAF	<i>Unidad de Análisis Financiero</i> (Financial Analysis Unit)
UD	<i>Unidades de Desarrollo</i> (Indexed Units)
WTO	World Trade Organization

GLOSSARY

In January 2001, the Committee on Payment and Settlement Systems (CPSS) of the Bank for International Settlements (BIS) published a combined glossary for payments and securities clearance and settlement terms. The glossary can be found on the BIS web page at www.bis.org. Based on this glossary, the Western Hemisphere Payments and Securities Clearance and Settlement Initiative (WHI) also produced a uniform glossary of terms in Spanish in order to avoid an unnecessary proliferation of terms and definitions. The Spanish glossary can be found on the WHI web page at www.ipho-whpi.org.

The following are some terms specific to the Costa Rican context:

<i>Destination Client:</i>	The person or firm that receives a transaction through its financial entity (destination entity).
<i>Destination Entity:</i>	A SINPE participant that receives a transaction.
<i>Originating Client:</i>	The person or firm that instructs its financial entity (origin entity) to make or to collect a payment.
<i>Originating Entity:</i>	A SINPE participant that initiates a transaction.
<i>Reserve Account:</i>	A deposit account that financial institutions and others hold at the BCCR for monetary policy and payment system purposes. Current accounts are authorized and regulated by the Board of Directors of the BCCR.
<i>Repurchase:</i>	A repurchase is similar to an ordinary repo. In a repurchase the securities underlying a transaction are pledged as collateral in a trust created and managed by the BNV for this specific purpose.

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