

STRICTLY CONFIDENTIAL

**AGREEMENT RELATING TO PAST SALES OF INTEREST RATE
HEDGING PRODUCTS**

("the Agreement")

- Parties:**
- (1) **THE FINANCIAL SERVICES AUTHORITY**
("the FSA"), of 25 The North Colonnade, Canary Wharf,
London, E14 5HS
- (2) *[NAME OF FIRM]*, of *[insert address]* ("the Firm")

together "the Parties".

Date: June 2012

Recitals:

- (A) The FSA has found evidence of poor practices in the Firm's sale of interest rate hedging products (as defined in Clause 15 below) to retail clients or private customers (as defined in the FSA's Glossary of Definitions for the purposes of the Conduct of Business sourcebook) on or after 1 December 2001 (the "**Relevant Business**"), and is concerned that such practices, combined with product complexity, customer sophistication and sales incentives may lead to poor outcomes for customers.
- (B) The Parties have conducted confidential settlement discussions in relation to the Relevant Business on a without prejudice basis.
- (C) The relevant FSA decision makers and *[insert name of CEO]* have approved the terms of this settlement between the Parties to this Agreement on behalf of the FSA and the Firm respectively.

Written Undertaking

1. The Firm will provide a written undertaking (“**Undertaking**”) to the FSA at the same time as executing this Agreement.
2. The Undertaking shall be in the form set out in Annex A.

Publication

3. The Firm agrees that the FSA may publish statements substantially in the form set out in Annex B relating to the subject matter of the Undertaking at any time on or after 29 June 2012 (“**Intended Publication Date**”), and that the FSA may publish any other statements relating to the subject matter of the Undertaking.
4. The Firm agrees that:
 - (a) it will not publish any public statement relating to the subject matter of the Undertaking before the Intended Publication Date;
 - (b) it will not publish any public statement relating to the subject matter of the Undertaking on the Intended Publication Date unless the statement has first been agreed by the FSA; and
 - (c) if, after the Intended Publication Date, the Firm wishes to publish a public statement relating to the subject matter of the Undertaking, it will give the FSA at least 48 hours notice of the fact that the statement is to be issued (except in an urgent situation or as required by law, in which case as much time as is reasonably possible will be provided), and at the same time, provide a copy of the draft statement to the FSA for the purposes of agreeing the form or content of the statement.
5. The Parties agree that all future statements or actions (including any responses to questions) relating to or connected with the subject matter of the Undertaking will be consistent with the content of this Agreement and the Undertaking generally.

Future Action

6. Nothing in this Agreement prevents or in any other way limits the FSA from taking disciplinary action or taking any other regulatory action in respect of any matter or business involving the Firm.

Without Prejudice

7. The Parties confirm that the negotiations and related correspondence prior to this Agreement are confidential and have been conducted and/or written on a without prejudice basis.

No Precedent

8. This is a unique solution to a specific set of FSA concerns. It is agreed between the Parties that nothing in this Agreement or the discussions to date, including all related correspondence, is to be regarded as establishing a precedent for the FSA's approach in the event of similar matters or issues arising in respect of other aspects of the Firm's business.

Rights of persons other than the Parties

9. A person who is not a Party to this Agreement has no right under the Contracts (Rights of Third Parties) Act 1999 or otherwise to enforce any term of this Agreement.

Governing Law

10. This Agreement is governed by and shall be construed in accordance with the law of England and Wales. The courts of England shall have exclusive jurisdiction to settle any claim, dispute or matter of difference which may arise out of, or in connection with this Agreement.

Confidentiality

11. The terms of this Agreement are confidential between the Parties and their legal advisers and shall not be disclosed to any third party except as envisaged in this Agreement, to the extent required by law or to ensure, enable or enforce compliance with this Agreement. Further, the Firm may disclose the terms of this Agreement to its auditors. The Firm shall obtain the prior written consent of the FSA before disclosing the terms of this Agreement to any other third party.

Entire Agreement

12. This Agreement constitutes the entire agreement between the Parties, and supersedes any previous agreement between the Parties and any of them relating to the subject matter of this Agreement. The Agreement may be varied or modified only by the written agreement of the Parties.

Counterparts

13. This Agreement may be executed in any number of counterparts, each of which, when executed, shall be an original, and all the counterparts together shall constitute one and the same instrument.

Definitions and Interpretation

14. Except where otherwise provided in this Agreement, terms used in this Agreement have the meaning given to them in FSMA and the FSA's Glossary of Definitions.

15. In this Agreement, a reference to:

- (a) 'interest rate hedging product' means a derivative (as defined in the FSA's Glossary of Definitions), which is separate to a lending arrangement and is for the purpose of managing interest rate fluctuations;

- (b) a document is a reference to that document as modified or replaced from time to time;
- (c) a person includes a reference to a corporation, association or partnership;
- (d) a person includes a reference to that person's legal representatives, successors and permitted assigns;
- (e) the singular includes the plural and vice versa.

Signed by: Dated.....

[insert name of CEO]

Duly authorised to sign for and on behalf of *[insert name of Firm]*

Signed by: Dated.....

For and on behalf of the FSA

ANNEX A – DRAFT WRITTEN UNDERTAKING

[On Firm's letterhead]

Financial Services Authority
25 The North Colonnade
Canary Wharf
London
E14 5HS

For the attention of: *[insert name of Supervisor(s)]*

Dear Sirs

WRITTEN UNDERTAKING IN RELATION TO INTEREST RATE HEDGING PRODUCTS

The defined terms used in this undertaking are set out in the attached Appendix.

We, *[insert name of Firm]* undertake to the FSA that, as soon as reasonably practicable after our receipt of a written notice from the FSA under section 166(1) of the Financial Services and Markets Act 2000 (“Section 166 Notice”) in relation to the matters contained in this undertaking, we will:

- (a) carry out a review in accordance with the terms set out in the Appendix. This will include:
 - (i) providing proactive redress to all Customers who do not meet the Sophisticated Customer Criteria to whom we sold Structured Collars (as defined in the Appendix) on or after 1 December 2001. Redress (whether in the form of cash payments or variation of contracts) will be determined and, if relevant, provided on the basis of what is fair and reasonable in the circumstances.
 - (ii) if, during the period of the Skilled Person’s appointment, we receive a Complaint from a Customer (who does not meet the Sophisticated Customer Criteria) in relation to the sale of a Cap made on or after 1 December 2001, reviewing the circumstances of the sale and determining and, if relevant, providing redress in the way described in paragraph (iii) below. If a Complaint

is received from a Customer after the period of the Skilled Person's appointment, that Complaint will be dealt with in accordance with our usual complaints handling process and, if applicable, DISP.

- (iii) carrying out a past business review of sales of all other Interest Rate Hedging Products to Customers made on or after 1 December 2001. This will include:
 - identifying Customers who do not meet the Sophisticated Customer Criteria;
 - writing to those Customers to ask if they want their sale reviewed;
 - carrying out file reviews for all Customers who indicate that they would like their sale reviewed to assess compliance with the Regulatory Requirements;
 - contacting Customers for information to supplement that which is held in our records;
 - carrying out an appropriate review exercise which will include taking into account all of the evidence and the individual circumstances of the customer;
 - if a breach of the Regulatory Requirements has occurred, determining and, if relevant, providing appropriate redress on the basis of what is fair and reasonable in the circumstances.

- (b) comply with the terms of the s.166 Notice and appoint a Skilled Person to report on our conduct of the review set out in paragraph (a).
- (c) with effect from the date of this undertaking, we will cease all marketing of Structured Collars to retail clients.

I, *[insert name of CEO]* confirm that I will have responsibility for oversight of *[insert name of Firm]*'s conduct of this review and will take reasonable steps to ensure that it operates in accordance with the terms set out in the Appendix. This will include ensuring that *[insert name of Firm]* treats its complainants fairly. I will ensure that *[insert name of Firm]* prioritises any Customers who are in financial difficulty and, except in exceptional circumstances, such as, for example, where this is necessary to preserve value in the Customer's business, will not foreclose on or adversely vary existing lending facilities

(without giving prior notice to the Customer and obtaining their prior consent) until [*insert name of Firm*] has issued a final redress determination and, if relevant, provided redress to that Customer.

Signed by:

[insert name of CEO]

Duly authorised to sign for and on behalf of
[insert name of Firm]

APPENDIX

TERMS OF PROACTIVE REDRESS EXERCISE AND PAST BUSINESS REVIEW

1. Definitions and Interpretation

- 1.1. Except where otherwise provided in this Appendix, terms used in this Appendix have the meaning ascribed to them in the FSA's Glossary of Definitions.
- 1.2. 'Cap' means an Interest Rate Hedging Product which enables a customer to restrict his exposure to interest rate increases to a maximum upper limit, with no lower limit.
- 1.3. 'Complaint' means any oral or written expression of dissatisfaction, whether justified or not, from, or on behalf of, a Customer about the provision of, or failure to provide, a financial service which alleges that the Customer has suffered (or may suffer) financial loss, material distress or material inconvenience.
- 1.4. 'Customer' means:
 - 1.4.1. in respect of sales made by the Firm on or before 31 October 2007, a person categorised by the Firm, at the time the sale was concluded, as a private customer for the purposes of COB 2 and COB 5 as defined by the version of the FSA's Handbook of rules and guidance then in force; or
 - 1.4.2. in respect of sales made by the Firm on or after 1 November 2007, a person categorised by the Firm, at the time the sale was concluded, as a retail client in accordance with COBS 3.4.1R.
- 1.5. 'Firm' means *[insert name of Firm]*.
- 1.6. 'Interest Rate Hedging Product' means a derivative (as defined in the FSA's Glossary of Definitions) which is separate to a lending arrangement and is for the purpose of managing interest rate fluctuations.
- 1.7. 'Redress determination' shall be construed in accordance with paragraph 3.
- 1.8. 'Regulatory Requirements' means the principles, rules and guidance contained in the FSA's Handbook.
- 1.9. The 'Sales Standards' are:
 - 1.9.1. In good time before conclusion of the contract, the Firm has provided the Customer with appropriate, comprehensible and fair, clear and not misleading information on the features, benefits and risks associated with the Interest Rate Hedging Product.

- 1.9.2. In good time before conclusion of the contract, the Firm has provided the Customer with an appropriate, comprehensible and fair, clear and not misleading disclosure of any potential break costs.
 - 1.9.3. The Interest Rate Hedging Product does not exceed the term or value of any lending arrangements without a legitimate reason, and if it does, the potential consequences have been disclosed to the Customer in a comprehensible and fair, clear and not misleading way.
 - 1.9.4. The Firm has had due regard to the information needs of the Customer and provided comprehensible, and fair, clear and not misleading information about the features, benefits and risks of relevant alternative Interest Rate Hedging Products.
 - 1.9.5. In relation to an advised sale:
 - 1.9.5.1. The Firm has obtained sufficient personal and financial information about the Customer, including the Customer's investment objectives, level of education, profession or former profession and relevant past experience of Interest Rate Hedging Products.
 - 1.9.5.2. The Firm has taken reasonable steps to ensure that the personal recommendation is suitable for the Customer.
 - 1.9.6. In relation to a non-advised sale, no advice has been given to the Customer during the sales process.
 - 1.9.7. In relation to a non-advised sale on or before 31 October 2007, the Firm has taken reasonable steps to ensure that the Customer understands the nature of the risks involved and provided the Customer with the relevant risk warning notice.
 - 1.9.8. In relation to a non-advised sale on or after 1 November 2007, the Firm has assessed whether entering into the Interest Rate Hedging Product is appropriate for the Customer by determining whether the Customer has the necessary knowledge and experience to understand the risks involved. The Firm has obtained information regarding the client's level of education, profession or former profession, and relevant past experience of Interest Rate Hedging Products.
- 1.10. 'Skilled Person' means the independent third party, approved by the FSA, who will report to the FSA under section 166 of the Financial Services and Markets Act 2000 on the Firm's conduct of the review.
 - 1.11. 'Sophisticated Customer Criteria' means:
 - 1.11.1. In the financial year during which the sale was concluded, a Customer who met at least two of the following:

- 1.11.1.1. a turnover of more than £6.5 million; or
- 1.11.1.2. a balance sheet total of more than £3.26 million; or
- 1.11.1.3. more than 50 employees;

or

- 1.11.2. The Firm is able to demonstrate that, at the time of the sale, the Customer had the necessary experience and knowledge to understand the service to be provided and the type of product or transaction envisaged, including their complexity and the risks involved.
- 1.12. ‘Structured Collar’ means an Interest Rate Hedging Product which enables a customer to limit interest rate fluctuations to within a specified range, but involves arrangements where, if the reference interest rate falls below the bottom of the range, the interest rate payable by the customer may increase above the bottom of the range.

2. Scope of review

- 2.1. The Firm will carry out:
 - 2.1.1. a proactive redress exercise in relation to its and its associates’ sales of Structured Collars to Customers who did not meet the Sophisticated Customer Criteria made on or after 1 December 2001 (“Category A Business”);
 - 2.1.2. a past business review of its and its associates’ sales of Interest Rate Hedging Products to Customers who did not meet the Sophisticated Customer Criteria which are not Structured Collars or Caps made on or after 1 December 2001 (“Category B Business”); and
 - 2.1.3. if, after the date of this undertaking and during the period of the Skilled Person’s appointment, it receives a Complaint from a Customer who did not meet the Sophisticated Customer Criteria in relation to the sale of a Cap made on or after 1 December 2001 (“Category C Business”), a review of that sale in accordance with the process for the Category B Business set out in paragraphs 3.10 to 3.16;

under which it will determine what redress should be provided and actions should be taken in respect of defined categories of customers.

3. Review process

Category A Business

- 3.1. The Firm will provide appropriate redress to all Customers of the Category A Business, other than those Customers determined to meet the Sophisticated Customer Criteria in accordance with the process set out in paragraph 3.2 below.

- 3.2. The Firm will identify any Customers of the Category A Business who, in its opinion, meets the Sophisticated Customer Criteria and notify the Skilled Person of these Customers. The Skilled Person will carry out an assessment of whether, in its opinion, each of those Customers meets the Sophisticated Customer Criteria. If, in the Skilled Person's opinion, a Customer did not meet the Sophisticated Customer Criteria, the Firm will accept that opinion and provide appropriate redress to that Customer. If, in the Skilled Person's opinion, a Customer did meet the Sophisticated Customer Criteria, the Firm will write to that Customer clearly explaining that:
- 3.2.1. the Customer is deemed to meet the Sophisticated Customer Criteria, together with the basis for reaching that conclusion;
 - 3.2.2. this means the Customer is not eligible for any automatic redress under the Firm's proactive redress exercise; and
 - 3.2.3. the Customer may make a Complaint to the Firm which the Firm will consider under its usual complaints handling procedures and, if applicable, DISP.
- 3.3. The Firm will determine the appropriate redress for each Customer who does not meet the Sophisticated Customer Criteria ("Relevant Category A Customer") on the basis of what is fair and reasonable in the circumstances, taking into consideration the following presumptions:
- 3.3.1. Where the Firm can demonstrate that a requirement to have interest rate protection was a legitimate condition of the lending arrangement or the Firm can demonstrate that the Customer had an express wish for interest rate protection, fair and reasonable redress will be replacing the Structured Collar with simple interest rate protection (e.g. a fixed rate loan) at the rate prevailing at the time of the sale and refunding any charges paid by the Customer in relation to the Structured Collar which would not have been payable had the Customer entered into a simple interest rate protection product.
 - 3.3.2. If the term of the Structured Collar exceeded the term or value of any relevant lending arrangements without a legitimate reason, fair and reasonable redress will include the difference between the amount the Customer paid and the amount the Customer would have paid if the Structured Collar had not exceeded the term or value of the lending arrangement.
 - 3.3.3. For all other Customers, depending upon their individual circumstances, fair and reasonable redress may include, but is not limited to, offering the Customer the option of exiting the Structured Collar at no cost, or at a proportion of the cost, and/or a refund of part or all of the charges paid by the Customer to date.
- 3.4. Before any redress is provided to Relevant Category A Customers, the Skilled Person will review the Firm's assessments of the appropriateness of redress and the fair and reasonable nature of the Firm's redress proposals. If the Skilled Person does not agree with any of the Firm's assessments, the Skilled Person will provide the Firm with reasons for that

disagreement and an explanation of why, in the Skilled Person's opinion, an alternative approach is needed. The Firm will then put forward an alternative redress proposal for the Skilled Person to review. The Firm will not issue a provisional redress determination to a Relevant Category A Customer until the Skilled Person has agreed with the fair and reasonable nature of the Firm's redress proposal.

- 3.5. The Firm will issue a provisional redress determination to each Relevant Category A Customer on the basis of the proposals agreed with the Skilled Person in paragraph 3.4. The provisional redress determination will specify why the redress is appropriate and refer to the fact that the redress proposal has been reviewed by an independent third party. If the Relevant Category A Customer accepts the provisional redress determination, the Firm will issue a final redress determination and provide redress in a prompt manner to the Customer in accordance with that redress determination. The Firm and the Customer may agree an alternative redress solution.
- 3.6. The final redress determination, or, if relevant, the letter sent to the Relevant Category A Customer following agreement of an alternative redress solution and review by the Skilled Person, will be treated as the Firm's final response for the purposes of DISP 1.6.2R and will inform the Customer that he may be eligible to complain to the Financial Ombudsman Service if he is dissatisfied with the Firm's redress determination, and must do so within six months.

Category B Business

- 3.7. The Firm and the Skilled Person will design the methodology for the past business review; this will include agreeing the information to be obtained from the Customer and will take into account the matters sets out in paragraphs 3.8 to 3.16 and paragraph 4. The proposed methodology will be reviewed by the FSA to ensure that it meets the key requirements set out in this Appendix. Once the methodology has been approved by the FSA, the Firm will carry out the review in accordance with that methodology.
- 3.8. The Firm will carry out a past business review in respect of the Category B Business on the following terms:
 - 3.8.1. the Firm will identify any Customers of the Category B Business who, in its opinion, meets the Sophisticated Customer Criteria and notify the Skilled Person of these Customers. The Skilled Person will carry out an assessment of whether, in its opinion, each of those Customers meets the Sophisticated Customer Criteria. If, in the Skilled Person's opinion, a Customer did meet the Sophisticated Customer Criteria, the Firm will write to that Customer clearly explaining that:
 - 3.8.1.1. the Customer is deemed to have meet the Sophisticated Customer Criteria, together with the basis for reaching that conclusion;
 - 3.8.1.2. this means the Customer is not eligible to request a review by the Firm under its past business review; and

- 3.8.1.3. the Customer may make a Complaint to the Firm which the Firm will consider under its usual complaints handling procedures and, if applicable, DISP.
- 3.8.2. the Firm will write to all Customers of the Category B Business who, in the Skilled Person's opinion, do not meet the Sophisticated Customer Criteria ("Relevant Category B Customer") clearly explaining in general terms any potential failings and inviting them to respond to the Firm if they would like the Firm to review its sale of the relevant Interest Rate Hedging Product. The letter will refer to the fact that the Customer may be entitled to compensation and the Customer will be asked to complete a simple standard form which will allow them to indicate that they would like their sale reviewed.
- 3.9. If a Customer does not respond to the letter sent by the Firm in paragraph 3.8.2, the Firm will send a further letter to that Customer containing the information set out in paragraph 3.8.2.
- 3.10. The Firm will review all sales of Interest Rate Hedging Products to Relevant Category B Customers who return the form to indicate that they would like their sale reviewed. This review will assess the compliance of the sale of the relevant Interest Rate Hedging Product with the Regulatory Requirements, taking into account, in particular, the Sales Standards. As part of this review, the Firm will take reasonable steps to contact each Relevant Category B Customer who responds indicating that they would like their sale reviewed in order to discuss the sale orally. The Firm will ensure that the reviews are not conducted by a person who was involved in the sale of the relevant Interest Rate Hedging Product.
- 3.11. The Firm will carry out an assessment of whether it is appropriate to provide redress to each Relevant Category B Customer who responds to indicate that they would like their sale reviewed. If the Firm concludes that it would be appropriate to provide redress to a Relevant Category B Customer, it will determine what redress would be fair and reasonable in the circumstances. Fair and reasonable redress may include, but is not limited to, offering the Customer the option of exiting the relevant Interest Rate Hedging Product at no cost, or at a proportion of the cost, and a refund of part or all of the charges paid by the Customer to date. It may also include offering the customer an alternative product (e.g. a fixed rate loan).
- 3.12. Before any redress is provided to Relevant Category B Customers, the Skilled Person will review each of the Firm's assessments of the appropriateness of redress and the fair and reasonable nature of the Firm's redress proposals, if relevant. If the Skilled Person does not agree with any of the Firm's assessments, the Skilled Person will provide the Firm with reasons for that disagreement and an explanation of why, in the Skilled Person's opinion, an alternative approach is needed. The Firm will then put forward an alternative redress proposal for the Skilled Person to review. The Firm will not issue a redress determination to a Relevant Category B Customer until the Skilled Person has agreed with the

appropriateness of the redress and the fair and reasonable nature of the Firm's redress proposal.

- 3.13. The Firm will issue a provisional redress determination to each Relevant Category B Customer on the basis of the proposals agreed with the Skilled Person in paragraph 3.12. The provisional redress determination will explain the basis for the conclusion on redress being due (or not) and (where relevant) how the redress has been determined. The provisional redress determination will refer to the fact that the redress proposal has been reviewed by an independent third party.
- 3.14. In all cases the Firm will issue a final redress determination to each Relevant Category B Customer.
- 3.15. If a Customer accepts the Firm's redress determination, the Firm will provide any redress due in a prompt manner to each Relevant Category B Customer in accordance with its redress determinations. The Firm and the Customer may agree an alternative redress solution.
- 3.16. The final redress determination, or, if relevant, the letter sent to the Relevant Category B Customer following agreement of an alternative redress solution and review by the Skilled Person, will be treated as the Firm's final response for the purposes of DISP 1.6.2R and will inform the Customer that he may be eligible to complain to the Financial Ombudsman Service if he is dissatisfied with the Firm's redress determination, and must do so within six months.

Category C Business

- 3.17. If, during the period of the Skilled Person's appointment, the Firm receives a Complaint from a Customer in relation to the sale of a Cap, the Firm will determine whether that Customer meets the Sophisticated Customer Criteria. The Skilled Person will carry out an assessment of whether, in its opinion, each Customer meets the Sophisticated Customer Criteria. If, in the Skilled Person's opinion, the Customer does not meet the Sophisticated Customer Criteria, the Firm follow the process set out in paragraphs 3.10 to 3.16. If, in the Skilled Person's opinion, the Customer does meet the Sophisticated Customer Criteria, the Complaint will be dealt with in accordance with the Firm's usual complaints handling procedures and, if applicable, DISP.
- 3.18. If a Complaint is received from a Customer in relation to the sale of a Cap after the period of the Skilled Person's appointment, that Complaint will be dealt with in accordance with the Firm's usual complaints handling procedures and, if applicable, DISP.

4. General

- 4.1. The Firm will agree with the FSA, in advance, the content of all customer communications and other key documents used in connection with the review undertaken pursuant to this Appendix.

- 4.2. The Firm will not make any communication to a Customer which seeks to influence for the benefit of the Firm the outcome of the processes undertaken pursuant to this Appendix.
- 4.3. The Firm will put clear and appropriate information on its website to explain how Customers of the Category A Business who do meet the Sophisticated Customer Criteria and Customers who entered into a Cap can make a Complaint to the Firm. This will include information about the timescale within which Customers who entered into a Cap would need to complain in order for the Firm to review their Complaint using the process set out in paragraphs 3.11 and 3.16 and explain that any Complaints received after this time will be dealt with by the Firm in accordance with its usual complaints handling procedures without the involvement of an independent third party.
- 4.4. The Skilled Person will provide a report to the FSA in accordance with the terms of the Section 166 Notice.
- 4.5. The Firm will provide regular updates to the FSA on the conduct of the review exercise.