Dear Sir,

Following the FSA’s annual review of Regulated Covered Bond programmes conducted last year, specific feedback was provided to a number of issuers on the scope and depth of engagement that the Compliance function has with the programme.

In addition to this, in June 2011 the RCB team sought the views from all registered issuers on the nature of the interaction between Compliance and their regulated covered bond programmes.

Taking into account the feedback received and our observations we are writing to more fully set out our expectations of the involvement the Compliance function should have with regulated programmes for the benefit of issuers.

As signatory of the RCB ID Annual Attestation of Compliance for the regulated covered bond programme we expect you to ensure that the arrangements relating to the management of the programme – including the governance and oversight arrangements meet the expectations set out by the FSA.

We recognise that the specific role carried out by the compliance function may vary between issuers, with certain aspects of oversight shared between other second line functions. Below, we set out our expectations and provide examples of areas of good practice that we have observed. You should consider whether you should enhance the second line oversight of your programme in light of the examples below.

The effectiveness of the second line engagement with the programme will continue to be assessed in future annual reviews.

**FSA Expectations**

We expect that the second line oversight of all Regulated issuers should include the following at a minimum:

- Clearly defined and documented mandate and terms of reference related to the programme and regular formalised interaction with the programme.
• Ongoing monitoring of the programme (e.g. checks accuracy of regulatory and investor reporting, aware of and monitoring breaches).

• Clear understanding of RCB requirements, and the role of the compliance function in relation to the programme. Appraised of relevant regulatory developments, and able to provide advice internally as appropriate.

• Adequate and skilled resource, with appropriate depth of expertise in covered bonds, evidence of ability to challenge management.

• Clearly defined escalation process i) from first line to compliance and ii) from compliance to independent risk oversight committees.

Examples of good practice observed
We have observed the following good practice by issuers of Regulated Covered Bonds

• Compliance is represented as voting member on covered bond management committees and relevant steering groups with full access to relevant minutes and MI.

• Compliance representatives have detailed knowledge of the product and offer robust challenge to the first line, for example, highlighting any anomalies or errors in investor reporting before publication and seeking clarification of the underlying reasons.

• Compliance undertakes regular reviews of the programme, with clear channels of escalation between i) first line and compliance function, ii) independent upwards escalation of issues from the compliance function and senior committees

• Compliance undertakes active ‘horizon scanning’ and provides advice on changes in regulatory environment and is engaged in providing responses to regulatory changes.

• Compliance sign off of applications for regulated status and material change proposals

Please do not hesitate to contact any member of the regulated covered bond team or your supervisor if you have any questions, or wish to discuss the points raised in this letter further.