



Transparency report to the shareholders of UBS AG

Financial market crisis, cross-border wealth management business, liability issues and internal reviews

Contacts

Investor Relations

Hotline Zurich +41-44-234 4100
Hotline New York +1-212-882 5734

UBS AG, Investor Relations
P.O. Box, CH-8098 Zurich, Switzerland

sh-investorrelations@ubs.com
www.ubs.com/investors

Media Relations

Zurich +41-44-234 8500
mediarelations@ubs.com

London +44-20-7567 4714
ubs-media-relations@ubs.com

New York +1-212-882 5857
mediarelations-ny@ubs.com

Hong Kong +852-2971 8200
sh-mediarelations-ap@ubs.com

Shareholder Services

Hotline +41-44-235 6202
Fax (Zurich) +41-44-235 3154

UBS AG, Shareholder Services
P.O. Box, CH-8098 Zurich, Switzerland

sh-shareholder-services@ubs.com

Imprint

Publisher: UBS AG, Zurich and Basel, Switzerland
Language: English and German
SAP-No. 83436E

© UBS 2010. The key symbol and UBS are among the registered and unregistered trademarks of UBS. All rights reserved.

Printed in Switzerland on chlorine-free paper with mineral oil-reduced inks. Paper production from socially responsible and ecologically sound forestry practices.



Mixed Sources
Product group from well-managed
forests and other controlled sources
www.fsc.org Cert no. SQ5-COC-100112
© 1996 Forest Stewardship Council



Dear Shareholders, Dear Readers,

A number of recent events have given rise to heightened public interest in the inner workings of UBS – the enormous losses incurred in connection with the global financial crisis, legal disputes with US authorities, and the rescue efforts undertaken by the Swiss Confederation and the Swiss National Bank. Above all, the fact that the Swiss government was obliged to step in as an interim shareholder in UBS has given rise to public demands for clarification as to what actually took place inside the bank. Voices have also been raised calling for the responsible persons to be held to account. The Board of Directors fully agrees that transparency is essential if UBS is to regain public trust.

In their report of 30 May 2010, the Control Committees of Switzerland's Federal Parliament requested that UBS undertake specific steps to assess the manner in which the financial market crisis and issues relating to the bank's cross-border business in the US were dealt with internally. UBS was further asked to explain in terms that would be comprehensible also to the general public its decision to refrain from prosecuting criminal and civil claims against former members of UBS's senior management. Finally, UBS was advised to inform the public as to its principal findings and conclusions.

This transparency report is our response to the Parliamentary Control Committees' recommendations to UBS, which were seconded by the Swiss Federal Council, the Swiss government's highest executive body. The report provides a full description of the circumstances inside UBS that were behind the financial losses and legal disputes of recent years, the lessons that the bank has learned from these experiences, and the measures taken both to remedy the situation and to prevent its recurrence. We also explain the reasons behind the UBS Board of Directors' decision not to take legal action against the bank's former directors and officers. We are convinced that the investigations conducted both by UBS itself and by various regulatory authorities have succeeded in shedding full light on the internal causes that gave rise to the serious predicament in which the bank found itself. This report completes the process of achieving full transparency. It has been written with a view to responding to the need of all those with a stake in UBS's future to understand what took place.

Negative public opinion

Prior to the crisis, UBS had a reputation as a successful and prudently managed bank. Many Swiss citizens may even have taken pride in the fact that a company with such high global prestige, and so seemingly solid, had its headquarters and its roots in Switzerland. In the aftermath of the financial market crisis it was revealed, however, that UBS had taken a serious turn in the wrong direction under the leadership of the senior management then in charge of the bank. The result was an enormous loss of trust.

We appreciate the fact that many people were deeply dismayed at these events. We also understand fully the questions

that have been raised in public: Who is responsible for the bank's losses and for its inappropriate conduct in the US? Should the responsible persons be punished and, to the extent possible, compelled to make good the damage that was caused? How was it even possible that such a seemingly successful company could find itself in such a situation? Is the present Board of Directors attempting to whitewash the acts and omissions of the persons to blame by not taking legal action against them?

These questions are all the more justified in view of the Swiss Confederation's having used taxpayer money to provide UBS with capital and the Swiss National Bank's having been compelled to assume some of UBS's risk positions. The fact that the Swiss Confederation has, in the interim, been able to sell its UBS holdings with a respectable profit and that the Swiss National Bank may well come out a winner on the positions it acquired, changes nothing in this regard. The Swiss Parliamentary Control Committees and a delegation of the Federal Council have also made clear that they expect UBS to bring clarity to these questions.

Confronting the past

In 2009, a substantially recomposed Board of Directors, together with a new Group Executive Board, took on the challenge of restructuring UBS and putting it back on the path to sustainable success. As we carry out this endeavor, our focus is squarely on the future, using the lessons of the past to confront the complex economic and regulatory environment that will shape the years to come. With this in mind, coming to terms with its recent past was clearly also in the company's own best interest.

In reviewing the issues and preparing our decisions, we have relied on comprehensive investigations conducted by the bank itself, on legal opinions prepared by outside experts both from Switzerland and abroad, and on the investigations conducted and reports issued by the regulatory authorities. The cost of these extensive internal and external investigations ran into the hundreds of millions of Swiss francs. They have been documented by dozens of reports comprising thousands and thousands of pages. The lessons we have learned from these intensive efforts have been, and will continue to be, put into practice both in the bank's overall strategy and its day-to-day business operations.

The internal and external investigations also provided the Board of Directors with important insights concerning questions of liability. The Board's decision to refrain from taking legal action is based on solid grounds. First, as this report shows, the likelihood of success in such litigation is highly uncertain. Second, experience shows that such proceedings generally go on for years, entailing horrendous costs and giving rise again and again to damaging headlines that render the task of rebuilding trust even more difficult – particularly if the final outcome is less than successful. Moreover, lawsuits against individuals are of no help in getting to the bottom of the underlying causes of a crisis. Such litigation would paralyze many of the bank's resources and

hinder it in orientating itself toward the future. Finally – and this was a consideration that weighed particularly strongly – such proceedings would significantly weaken the position of UBS in legal proceedings currently pending in the US. Taking on such financial risks in the name of UBS would be highly irresponsible.

For these reasons, the Board of Directors considers that bringing litigation against former directors and officers of the bank is not an option. This must be stated unequivocally. The Board of Directors believes that it has no discretion in this matter: not to take legal action is the only possible decision in this matter that is compatible with the Board's duties to UBS and its shareholders – even if sections of the public may think otherwise.

Transparency

This report sets forth the reasons behind the Board of Director's decision with regard to litigation against the bank's former leadership. We are convinced that this report provides all of the relevant information on the issue and satisfies the need of all stakeholders for full and total transparency.

In order to provide both the public and shareholders with an independent second opinion, we have commissioned a report from Prof. Dr. Peter Forstmoser, an authority in the field of company law. Prof. Forstmoser independently assessed whether the decisions taken by the Board of Directors are, in fact, tenable.

In addition, we believe that both UBS's shareholders and its top management are entitled to an independent assessment of the reasons that led to a company as reputable as UBS becoming so mired in difficulties. In this connection, it is important to evaluate UBS's strategy and actions in the context of both the general economic environment in the period leading up to the global financial crisis and of the behavior of other financial institutions. This assessment has been undertaken by Dr. Tobias Straumann, Lecturer at the University of Zurich, a specialist in the history of financial markets. Dr. Straumann, as well, enjoyed full independence in the preparation of his report.

Responsibility

What happened should not have happened. The present report sheds light on the inappropriate behavior and failings that made it possible. Notwithstanding our decision to refrain from taking legal action, we have no wish to gloss over the mistakes that were made, nor do we desire to discharge the persons in charge from their entrepreneurial responsibility. All those who stood at the helm of UBS at the time in question must face up to the moral responsibility they bear, even if the questions of criminal or civil liability remain unresolved. Many of those who led UBS at the time have already acknowledged this responsibility toward the company, either by waiving certain compensation claims or by repaying amounts received.

Switzerland as a headquarters for globally active businesses

Switzerland, although a small country, has attained a higher than average level of prosperity. This is a product not only of the

proficiency of Switzerland's business professionals, but also of the country's outstanding environment for doing business. The creation of this environment is the accomplishment of our political institutions.

Because of this favorable business environment, UBS and its predecessor banks were able to develop, over a period of many years, into a company of great significance for the entire Swiss economy and its financial industry. This is the expression of an important reciprocal relationship: high-performance companies contribute to Switzerland's prosperity, and a favorable regulatory environment for business provides high-performance companies with the support base they require. The UBS Board of Directors is acutely aware that Swiss companies benefit to a high degree from being domiciled in Switzerland, and hence also bear a responsibility toward the country. When a large corporate group of global dimensions stumbles, this harms not only its own reputation, but also that of the place in which it is domiciled. The experience of UBS is a case in point.

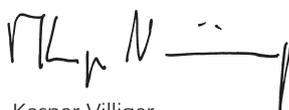
The principal reason for our decision to refrain from taking legal action against the persons formerly in positions of responsibility in the group was to protect the bank's own best interest. Nevertheless, the Board of Directors is also cognizant of its responsibility toward the country in which it is headquartered. For this reason, among others, UBS has systematically and unflinchingly drawn the necessary conclusions from its past mistakes. UBS has undertaken to establish a corporate culture that precludes any conduct that could cause harm either to the company or to the country it calls home, Switzerland. Similarly, we are convinced that refraining from litigation is very much in the long-term interests of Switzerland as an international business location. For UBS to take on the considerable risks involved in litigation, preventing it from resuming normal business operations for years to come, would be of benefit to no one.

Acknowledgements

The Board of Directors and the Group Executive Board owe a large debt of gratitude to the Swiss Parliament, the Federal Council, the Federal Administration and the Swiss National Bank. Our particular thanks go also to the shareholders and clients who have remained loyal to UBS in difficult times, and to all our employees, who have demonstrated their full commitment under demanding conditions.

UBS should never again find itself in a comparable position. Today, UBS is financially stable. We will do our best to ensure that it performs its services for Switzerland and the Swiss economy, and for the other countries in which it does business, responsibly, and in keeping with the highest standards of quality. Until we have achieved this for all to see, we will not rest.

Zurich, in October 2010



Kaspar Villiger
Chairman of the Board of Directors

Contents

4	I. Overview	
15	II. The financial market crisis	
16	A. What led to UBS's losses during the financial market crisis?	
16	1. Financial products in the US real estate market	
17	2. UBS's exposure to the US real estate market	
18	3. Outbreak of the crisis	
19	4. Measures taken by UBS to strengthen its capital base	
20	B. How did UBS review the crisis?	
20	1. UBS investigations	
21	2. Business areas affected by losses	
22	3. How was it possible for the losses to occur?	
24	C. How did the supervisory authorities deal with the crisis?	
24	1. Investigation by the Swiss Federal Banking Commission	
25	2. Investigation by the SIX Swiss Exchange	
25	3. Investigations by foreign supervisory authorities	
26	D. What measures has UBS taken to ensure that such losses do not recur?	
26	1. UBS action plan	
27	2. Strategy	
27	3. Governance	
27	4. Risk management	
28	5. Risk control and financial aspects	
28	6. Funding and treasury management	
29	7. Remuneration	
31	III. US cross-border wealth management business	
32	A. How did the issues with the US authorities arise?	
32	1. UBS's cross-border wealth management business	
32	2. Legal framework	
33	3. UBS's US cross-border business between 2000 and 2007	
34	4. Contact by the US authorities	
35	B. How did UBS handle the situation?	
35	1. Investigation by Wachtell, Lipton, Rosen & Katz	
37	2. Internal disciplinary investigation by UBS	
37	3. Why did the problems in the US cross-border wealth management business occur?	
38	C. How did the supervisory authorities react to the events?	
38	1. Investigation by the Swiss Federal Banking Commission	
40	2. Investigations by the US authorities	
43	D. What steps has UBS taken to ensure that the problems do not recur?	
43	1. Exit from the US cross-border business/ US Settlement Execution Program	
44	2. Comprehensive measures to address and control risks associated with the Wealth Management & Swiss Bank cross-border business globally/Cross-Border Business Review Program	
46	3. Changes to the governance of Legal & Compliance	
47	4. Improvement of governance and of the control program relating to the implementation of the QI Agreement	
49	IV. Liability issues	
51	A. Claims under civil law against former directors and officers	
51	1. Preconditions for a director's liability claim under civil law	
52	2. Investigations commissioned by UBS	
53	3. Liability claims in connection with the financial market crisis	
53	4. Liability claims in connection with the US cross-border wealth management business	
54	5. Further considerations by the Board of Directors	
56	B. Steps against the former directors and officers of UBS under criminal law	
56	1. Expert report by Bär & Karrer	
56	2. Assessment by the public prosecutor's office of the canton of Zurich	
57	3. Assessment of the Board of Directors	
58	C. Decision by the Board of Directors	
59	V. Where does UBS stand today?	
60	A. Need for a new corporate culture	
61	B. Outlook	
65	Glossary	

I. Overview

From the middle of 2007 until the end of 2009, UBS AG (UBS) experienced the most serious crisis in its corporate history. It was able to overcome this turbulent period thanks, in particular, to the support of the Swiss Confederation and its authorities: In the fall of 2008, the Swiss National Bank (SNB) undertook to acquire securities held by UBS in an amount of up to 60 billion US dollars to relieve UBS's balance sheet. By the spring of 2009, the SNB StabFund, a special purpose vehicle established by the SNB, had acquired such securities in the total amount of 39.6 billion dollars. At the same time, UBS received a capital injection of 6 billion Swiss francs from the Swiss Confederation. The Swiss authorities decided to support UBS with these measures with a view to UBS's systemic relevance to the Swiss financial center and the economy in general. Official diplomatic efforts were required in order to help resolve conflicts with the US authorities in the context of the cross-border wealth management business.

Today, in October 2010, UBS is once again healthy and robust. In the fourth quarter of 2009, it returned to profitability, its equity position is solid and, compared to the situation at the outbreak of the financial market crisis, its balance sheet total and risks have been reduced by some 50 percent. In summer 2009, the Swiss Confederation was able to sell the UBS shares it had received in connection with the capital injection at a profit. By the end of June 2010, the SNB StabFund's total exposure had been reduced to 19.2 billion dollars.

As positive as these recent developments may be, however, they cannot obscure the seriousness of the situation into which UBS managed to bring itself during the crisis. Rather, the question arises how the financial market crisis could cause such huge losses for the bank and how UBS could have maneuvered itself into such a difficult position in connection with the US cross-border wealth management business. As discussed in this report, internal factors, primarily organizational shortcomings and the lack of adequate controls inside the bank led to UBS suffering substantial losses in connection with the subprime crisis. The problems UBS faced in connection with its cross-border wealth management operations resulted in part from the insufficient enforcement and the lack of adequate control of internal regulations, and in part from a corporate culture that did not address violations of regulations by individual employees vigorously enough. Although not directly related to each other, both issues materialized simultaneously, causing a serious loss of reputation and confidence in the bank.

What has transpired since the middle of 2007? How could these serious problems occur, and what has been done since that time? By publishing this report, it is UBS's intention to create the transparency required to faithfully answer all relevant questions.

Creating transparency

From March 2009 to the end of May 2010, the Control Committees of the Federal Assembly (CCs) conducted an extensive

investigation into the conduct of the Swiss authorities under the pressure of the financial market crisis and into the surrender of UBS client data to the US by Swiss authorities. The CCs' report of 30 May 2010 includes, among others, 19 recommendations to the Federal Council for further action. Recommendation 19 is addressed directly to UBS and essentially requests the following:

- UBS shall ensure that the handling of the subprime crisis by the bank and its US cross-border business are investigated;
- the UBS Board of Directors shall create transparency with respect to the decision not to take criminal or civil legal action against former UBS management; and
- UBS shall inform the public of the essential findings and conclusions.

This report represents UBS's response to Recommendation 19 of the CCs and creates transparency with respect to the developments that occurred in recent years, the internal and external investigations that were conducted, and the measures implemented by UBS. Further, the UBS Board of Directors explains in this report to shareholders and the interested public its decision not to take legal action against former directors and officers.

This report has been prepared pursuant to instructions by the Board of Directors. In addition, the Board appointed two independent experts each with the mandate to prepare separate expert opinions.

- The first of these experts, Prof. Peter Forstmoser, professor emeritus at the University of Zurich and an authority in the field of corporate law, assessed the question of directors' liability under corporate law. Prof. Forstmoser specifically examined whether the decision of the Board of Directors not to take legal action against former members of management is defensible and whether the Board had at its disposal sufficient information on which to base such a decision.
- The second expert, Dr. Tobias Straumann, a private lecturer at the University of Zurich and economic historian specializing in financial markets, investigated the causes of the financial market crisis and of UBS's problems with its cross-border wealth management business in the US from an economic, historical and political perspective. Dr. Straumann also has extensive experience in analyzing international financial history and European monetary and economic policy. In his analysis, he considers the question of why UBS was particularly hard hit by the subprime crisis and what caused the undesirable developments in the cross-border wealth management business.

Both of the independent experts had access to all relevant documents, in particular to all internal and external investigation reports and expert opinions referred to in this transparency report. They received no instructions or other conditions from UBS with respect to the scope or content of their work or the conclusions to be reached.

The financial market crisis

Developments

Between the third quarter of 2007 and the fourth quarter of 2009, UBS wrote down more than 50 billion francs. Most of these write-downs had to be made as a result of the global financial market crisis, which had its origins in the structured financial product business linked to the US residential real estate market.

Such financial products, which reflect the risks of the underlying mortgage loans, had been able to satisfy increasing demand from investors prior to the crisis, but had also become more and more complex over time. Financial institutions such as UBS were involved at various levels of the market and also carried such products on their own balance sheets. Triggered by an unexpectedly severe and swift collapse of prices in the US real estate market, the simultaneous occurrence of a number of extraordinary factors caused the market for these products to dry up within a very brief period of time, beginning in July 2007. The sharpness of the decline in the US market for structured financial products came as a surprise to most market participants, including UBS.

The Group Executive Board of UBS recognized the extent of the possible consequences for the business with securitized products linked to the US housing market only at the end of July 2007, by which time the markets were already under pressure. The chairman and the two full-time vice-chairmen of the Board of Directors of UBS (the so-called "Chairman's Office") and the Group Executive Board were informed as to the extent of the problems on 6 August 2007.

On 14 August 2007, UBS issued a market warning with regard to problems related to the impending crisis. On 1 October 2007, it reported on the write-downs that it had made in the third quarter, and on 10 December 2007 it announced a number of capital restructuring measures, including the issuance of a 13 billion franc mandatory convertible bond to one of the Singapore government's sovereign wealth funds and to an investor in the Middle East. This and two other measures, such as the sale of treasury shares and the payment of a stock dividend rather than a cash dividend, enabled UBS to increase its overall equity base by a total of 19.4 billion francs.

Further write-downs in the first half of 2008 made another capital increase necessary: on 1 April 2008, UBS approached its shareholders and in June 2008 was able to raise approximately 15 billion francs in additional funds through a public capital increase. This, however, was not yet the end of the crisis.

The financial market crisis reached its peak after the collapse of the US investment bank Lehman Brothers in September 2008. Central banks worldwide were compelled to provide massive liquidity injections to ensure the continued operation of the credit business in the interbank system, and a number of governments, including those of the US, Great Britain and Germany, ordered state capital contributions to banks for which they were directly responsible. Switzerland also provided funds to the banking system.

On 16 October 2008, UBS reached an agreement with the SNB to transfer part of its US and other securities to a special purpose vehicle formed by the SNB under the name SNB Stab-

Fund. UBS contributed to the equity of this special purpose vehicle an amount corresponding to 10 percent of the value of the transferred positions, combined with the option to repurchase these positions. To fund the equity contribution, and maintain at the same time the strong capital position of UBS, the Swiss Confederation subscribed mandatory convertible notes in the amount of 6 billion francs. In addition, it announced that it was prepared to guarantee new short- and medium-term interbank liabilities as well as money market transactions of Swiss banks, if required. From the fall of 2008 through the spring of 2009, securities totaling 39.6 billion dollars were transferred to the special purpose vehicle.

The International Monetary Fund estimates that by April 2010, banks worldwide had to write down approximately 2,300 billion dollars during the course of the financial market crisis. Hardest hit were the US banks Citibank and Merrill Lynch; however, UBS ranked third worldwide for highest total losses incurred and first among the banks in Europe.

Review of the events

Following the outbreak of the financial market crisis and its first losses, UBS began to investigate the causes that had led to these developments. The supervisory authorities closely followed UBS in the internal investigations conducted in this context. An internal UBS investigation, the results of which were published in summary form in April 2008, identified a number of institutional weaknesses that had caused UBS to be more strongly hit by the crisis than others:

- **Growth strategy:** In the summer of 2005, UBS had spun off a significant portion of its business in fixed income investment products into its subsidiary Dillon Read Capital Management (DRCM). At the end of 2005, the decision was made to develop, in parallel to DRCM, the same type of business inside the UBS Investment Bank, since UBS hoped to become one of the top banks in the world in this sector as well. First, however, the required resources had to be put in place, as many specialists in the meantime had joined DRCM. In retrospect, the growth strategy had not been planned systematically enough and it had been implemented without sufficient monitoring.

As a result, the growth strategy led to a situation in which both DRCM and UBS Investment Bank were investing in similar categories of investment products. Because DRCM was invested, inter alia, in products with low credit ratings, while UBS invested primarily in products assumed to be of high quality, too little attention was paid to the risk of a simultaneous collapse in the prices for all investment products.

- **No balance sheet limits:** Prior to the financial market crisis, the bank had not set any limits for its balance sheet total. Together with the other causes described herein, this made it possible to accumulate enormous holdings in US mortgage securities, the consequences of which were devastating when that business began to fall apart.

- **Low refinancing rates:** Up until the outbreak of the financial market crisis, it was not a problem for UBS to obtain credit and capital market funding at favorable terms. The short-term funding obtained from the markets could be made available within the bank at no additional risk premium,

irrespective of the risks that the individual business units planned to assume. The Investment Bank was thus able to make investments in the ostensibly safe US mortgage market while obtaining funding at very favorable terms. This strategy imploded when credit markets dried up in the financial market crisis, since the market conditions no longer allowed UBS to refinance on favorable terms.

- *False sense of security despite warning signs:* Toward the end of 2006, that is, less than one year prior to the outbreak of the financial market crisis, it became apparent that the growth in the US real estate market might be turning into a speculative bubble.

In spite of these signs, up until July 2007, the management of UBS Investment Bank was confident. It falsely believed, on the one hand, that its investments in mostly high-quality investment products with high credit ratings and presumably adequate downside protection were, in fact, safe. Based on the presumed high quality of the underlying securities, these products were rated AAA or AA, sometimes even higher as so-called super senior. Insofar as UBS was involved, on the other hand, in the purchase, bundling and resale of structured financial products, it believed that the holdings of investment products held in its “warehouse” could be sold at any time in the market. Because of these assumptions, which in retrospect turned out to be incorrect, UBS neglected to take additional measures to limit its risks in the US housing market.

- *No overall assessment of risk positions:* The management of UBS Investment Bank was aware of the individual positions held by business units that invested in US mortgage products or bundled and resold them. There was, however, no overall assessment of the entirety of the bank’s credit and default risks associated therewith.
- *Reliance on information from business units:* Up until the end of July 2007, the UBS Group Executive Board relied on the statements of the responsible heads of the business units to the effect that risk management and risk control were being performed correctly in the US mortgage market. It was not until the end of July 2007 that the management of the Investment Bank became fully aware of the risk positions. The Chairman’s Office of the Board of Directors and the Group Executive Board were informed of these developments on 6 August 2007.
- *Overreliance on statistical models:* In hindsight, it is clear that UBS specialists in the risk control area placed too much trust in statistical models. The bank also relied too heavily on the rating agencies and the ratings they issued for certain investment products. This model-based approach, which furthermore relied heavily on the assessment made by the rating agencies, ultimately shifted attention from the fundamental risks underlying the US housing market.
- *Remuneration:* The remuneration models used prior to the financial market crisis did not distinguish sufficiently between real added value created by above-average performance and income generated by exploiting market advantages, such as low funding costs. The incentive structure encouraged the generation of revenues without adequately considering the associated risks.

The supervisory authorities – in particular the former Swiss Federal Banking Commission (SFBC; today the Swiss Financial Market Supervisory Authority, FINMA) – conducted independent investigations. These were completed in September 2008 and publicly announced in mid-October 2008. In its overall assessment, the SFBC stated that it agreed with UBS’s analysis with respect to the shortcomings that had been identified. The SFBC stated further that UBS had inadequately identified, limited and monitored its subprime risks. This finding related in general to UBS’s governance, operational and control processes as a whole, although to differing degrees. The SFBC reached the conclusion that not all of the shortcomings listed, considered individually, were indicative of inadequate organization, poor management or deficient governance. The essential point, however, was the unsatisfactory result they produced in combination.

In summary, the SFBC noted that UBS as a whole, in its dealings in subprime securities, had failed to demonstrate irreproachable business conduct, as required under banking law, but that the then-responsible executives of the bank could not be held liable under supervisory law. As the SFBC, pursuant to long-standing and confirmed practice, does not review the fit and proper status of executives who have left their position, the same question did not come up in respect to directors and officers who already had resigned. The SFBC further noted that its investigation had revealed no information that would suggest that UBS managers had deliberately intended to cause damage to the bank, or had deliberately assumed incalculable risks solely for the sake of receiving higher bonuses. There was also no indication that the individuals responsible for risk control had, in fact, been aware of the risks that were assumed but had willfully turned a blind eye to them.

UBS shares the assessments resulting from this investigation. Since 2008, and in part still under its former leadership, UBS has taken a series of measures, of which the major part has already been implemented. These measures are aimed at substantially strengthening risk control processes, thereby preventing a recurrence of the losses suffered in the financial market crisis. They include the following:

- *Strategy:* The overall strategy of the bank was adjusted to focus on business transactions carried out on the basis of client instructions. At the same time, proprietary trading and the resulting risks were reduced. As an additional immediate measure, the CEO of the Investment Bank reviewed the portfolios of each business area in 2008. The Group Executive Board, together with the CEO of the Investment Bank, now ensures that periodic reviews are carried out at all levels, in order to ensure that there is a comprehensive risk assessment.
- *Corporate governance:* Since the beginning of the financial market crisis, UBS has fundamentally recomposed the Board of Directors and Group Executive Board. A significant number of the new members of these boards were recruited from outside the company. The experience they gained in other financial service companies now benefits UBS.

There is now a clear separation of responsibilities between the Board of Directors, on the one hand, and the Group Executive Board on the other. In July 2008, the Chair-

man's Office was abolished and replaced by Board of Directors' committees; at the same time a new Risk Committee was established, consisting exclusively of independent directors. In October 2008, additional new members of the Board of Directors were elected. In the spring of 2009, the Group Executive Board was again recomposed to allow the bank in its entirety a new start.

The Board of Directors bears ultimate responsibility with regard to strategy. It decides on the risk capacity and risk appetite of the group, as well as on the allocation of capital and balance sheet limits among the divisions. The Group Executive Board is directly responsible for implementing the strategy and for allocating the required resources to the business units. It is assessed based on risk-adjusted profit.

- **Risk management:** The recording of positions, their valuation, and the assessment of their risks and effects on the profit and loss account are now regulated on a group-wide basis. The bank introduced procedures to continuously monitor complex products and transactions so that concentrations of risk can be identified at an early stage. Each business unit must be able to explain its balance sheet (including risk positions) and its profit and loss account based on standardized measurements.

Business plans are now assessed based on uniform criteria both at the group level and the level of the individual business units and are regularly scrutinized. Whether set targets can be achieved is reviewed at least four times per year by the CEO and the Group Executive Board. In the framework of reporting, the income and expenses of the individual business units are compared with projections, enabling corporate management to identify and correct undesirable developments early on.

- **Risk control and finance:** Prior to the financial market crisis, specialists, such as those in the area of risk control, often had two superiors – the head of the business unit as line manager and a specialist in the area of risk control; however, structures have now been simplified and harmonized. Each Chief Risk Officer of a business unit has now the Group Chief Risk Officer as the only direct superior, and the risk control function of the group is now independent of the business divisions.

The risk control rules and methods internally applied by the bank have been thoroughly reviewed and improved where necessary. This applies in particular to value-at-risk calculations, stress tests, risk aggregation and the monitoring of valuation and accounting models. The quality and frequency of reporting for the bank's profit and loss statement have also been increased. The harmonized and integrated internal reporting system now provides a "Monthly Performance Update" to all members of the Board of Directors and the Group Executive Board. This report analyzes the bank's business performance and sets out in detail the relevant internal and external risks to which the bank is exposed.

Entering into new businesses (New Business Initiatives) is now subject to more stringent controls and has to be submitted to the Risk Committee of the Board of Directors for approval. Committees have been formed at various levels to examine and approve large and high-risk transactions.

- **Fund-raising and balance sheet management:** The Group Executive Board now also constitutes the Asset and Liability Committee (ALCO) at the group level. The responsible members of this committee are accountable to the Board of Directors for the assigning of balance sheet limits, risk-weighted assets and capital to the individual business units. ALCO also approves internal group financing.

Limits for total balance sheet growth and risk-weighted assets have been introduced both on the group level and in particular at the level of the Investment Bank. Financing costs are now handled on the basis of risk.

- **Remuneration:** The remuneration of the members of the Board of Directors and Group Executive Board was reviewed and amended on the basis of the bank's goal of sustainable performance.

All aspects of individual target setting and performance review of the top managers of the bank have been improved. This was to ensure that managers, when making decisions regarding remuneration, place greater emphasis on sustainable increases in corporate value than was the case prior to the crisis. In addition, the remuneration will be provided increasingly in the form of shares and equity-related instruments.

Finally, UBS has reformed its basic remuneration principles. Contrary to the situation prior to the financial market crisis, variable compensation no longer contains only a bonus component, but in some cases also a malus component. In particular, a malus is recorded if a loss results at the group or division level, or if drastic adjustments to the consolidated balance sheet are required. A malus may also be recorded for individual managers where gross violations of compliance regulations or of risk guidelines are identified. In particularly severe cases, deferred remuneration is forfeited in its entirety.

A detailed explanation of the reasons leading to the losses that UBS suffered during the financial market crisis is provided in Part II.A (cf. below page 16 ff.) of this transparency report. Information on the investigations conducted by UBS into the reasons for the losses during the financial market crisis follows in Part II.B (cf. below page 20 ff.). The investigations conducted by domestic and foreign supervisory authorities in this regard are discussed in Part II.C (cf. below page 24 ff.). Finally, Part II.D (cf. below page 26 ff.) provides a detailed description of the steps that UBS has undertaken to ensure that the deficiencies that occurred in the past will not recur.

Cross-border wealth management business

Developments

UBS serves a large number of its clients via branch offices in their countries of residence. This business is referred to as "on-shore business". Other clients have an account with a UBS branch office or with a subsidiary of UBS outside their country of residence. This business is referred to as "offshore" or "cross-border" business. Cross-border business was and is an important line of business for UBS and many other banks, especially Swiss banks active in the area of international investment advi-

sory services and wealth management. When performing its cross-border business from Switzerland for US clients, UBS had to observe both Swiss law and the law of the country where the clients were located, that is, US law.

Many offshore clients choose to establish banking relationships with Swiss banks due to the political stability of the country and the high quality of services provided in the banking industry. For reasons of personal confidentiality, other clients place special value on the Swiss banking system and the bank-client confidentiality provided for in the Banking Act. Certain clients were also concerned with avoiding taxes in their country of residence. This was the root of the problem that led to the disputes between UBS and the US authorities.

In the late 1990s, the US tax authorities (the "Internal Revenue Service", or "IRS") revised the existing US withholding tax system in many respects and introduced the so-called "Qualified Intermediary System (QI System)". The intention of the IRS under the QI System was to ensure that income derived by non-US taxpayers from US securities would be subject to the proper withholding tax rates according to the applicable double taxation treaties (DTT). Further, the intention was that US taxpayers properly report and pay taxes on income generated from US securities held through non-US financial institutions.

The QI System is based on an agreement (the "Qualified Intermediary Agreement" or "QI Agreement") which foreign banks can conclude with the IRS. For non-US financial institutions subject to the QI Agreement the following applies: their clients who are US taxpayers can only hold their securities accounts under the scope of financial privacy in Switzerland if they do not invest in US securities through such accounts. Clients who are US taxpayers subject to US taxes and who wish to invest in US securities must submit to the foreign financial institution a so-called IRS Form W-9 that results in the disclosure of the client's account to the IRS. The banks are also obliged to perform certain administrative tasks for the IRS necessary for the correct application of the withholding tax rates to income generated from US securities held by non-US taxpayers pursuant to the applicable DTTs, in particular the identification of the beneficial owners of the US securities.

The QI Agreement between the IRS and UBS entered into force on 1 January 2001. UBS implemented the agreement and the necessary organizational measures in a timely manner, which required enormous efforts. As it later transpired, implementation at UBS was deficient, and, in a number of cases, the internal guidelines issued by the bank in connection with the QI Agreement were ignored. Insufficient controls led to these incidents being detected and sanctioned only at a much later date.

In addition to the provisions of the QI Agreement, UBS also had to comply with restrictions imposed by US financial market supervisory laws. Providing investment advice, wealth management or security trading services in the US is subject to a licensing requirement. The license requirement also applies to the cross-border business, in particular when clients are in the US, irrespective of whether they are contacted in person or by telephone, fax, post or e-mail. Prior to 2005, UBS was not licensed in the US for its cross-border wealth management business and was therefore subject to the restrictions resulting from the license requirement (SEC Restrictions). Before obtaining a

license, UBS was not permitted, for example, to accept orders for the purchase or sale of shares on US territory or to provide investment advice to its clients in the US. As the investigations revealed, certain client advisors in a number of cases ignored the SEC Restrictions, in violation of internal guidelines.

In September 2007, the US Department of Justice (DoJ) and later the US Securities Exchange Commission (SEC) informed UBS that they had opened investigations into the bank's activities after being made aware by Bradley Birkenfeld, a former UBS client advisor, of alleged irregularities in the US cross-border business. Specifically, both authorities asserted that UBS had tolerated, in numerous instances, the violation of SEC Restrictions, and that, in connection with the implementation of the QI Agreement, there had been circumventions with respect to clients subject to US taxation. At the end of February 2008, the DoJ requested that information relating to certain account relationships with US clients in Switzerland, including the clients' identity, be disclosed. The IRS complemented these information requests of the US authorities in June and July 2008 first with a so-called John Doe Summons, and then with a request for administrative assistance submitted to the Swiss Federal Tax Administration (FTA) under the DTT between Switzerland and the US. On 17 July 2008, the Permanent Subcommittee on Investigations of the United States Senate held a public hearing on UBS's US cross-border wealth management business. As from March 2008, UBS sought the assistance of the Swiss government. The investigations subsequently carried out by UBS, the SFBC and the US authorities, and the administrative assistance proceedings carried out by the FTA, proved to be time-consuming. In retrospect, both UBS and the Swiss government did not inform each other sufficiently about the increasing escalation of the matter and they both equally failed to accurately assess the political situation in the US. Only relatively late in the process was a committee of the Board of Directors mandated to closely supervise the handling and resolution of the matter. The investigations carried out by UBS, the SFBC and the US authorities ultimately established that, from 2001 through 2007, UBS and its employees had breached obligations under the QI Agreement and the SEC Restrictions, and that the bank had failed to sufficiently control compliance with these restrictions and obligations.

Upon conclusion of the investigations by UBS and the SFBC, UBS and the US authorities started negotiations regarding a potential settlement. The negotiations with the DoJ proved to be very difficult. The US authorities, among others, took the position that the conclusion of a settlement would only be possible if there was a simultaneous delivery of account documents relating to a number of client accounts, either in the course of the ongoing administrative assistance proceedings in tax matters, or otherwise. At the same time, there was a threat of a criminal indictment of the bank and its top corporate bodies. UBS informed the SFBC, its successor authority FINMA and the Federal Council regularly as to the course of these negotiations. In light of the foreseeable conflict between the two jurisdictions, the Swiss authorities took up direct contact with the US authorities beginning in the spring of 2008. On 18 February 2009, UBS was finally able to reach settlements with the DoJ and the SEC. As part of these settlements, UBS agreed to pay a total of

780 million dollars and to complete the exit of the US cross-border business which it had already begun. Further, in view of the threat of a criminal indictment in the US and of its potential effects on the bank, FINMA instructed UBS to hand over to it data concerning certain client relationships, which FINMA then passed on to the DoJ. Despite intensive efforts undertaken towards the end of 2008 and the beginning of 2009, it was not possible to settle the John Doe Summons proceedings with the IRS contemporaneously with the settlements concluded with the DoJ and the SEC.

The negotiations with the IRS concerning the John Doe Summons proceedings continued into the summer of 2009. The IRS had commenced these court proceedings with the objective to forcing UBS to turn over all client data related to UBS accounts maintained by US taxpayers in Switzerland. Switzerland and the US managed to settle these proceedings on the basis of a treaty on 19 August 2009. On the basis of this treaty, the IRS submitted a request for administrative assistance to the Federal Tax Administration based on the existing double taxation agreement between the two countries. The purpose of this request was to obtain information concerning certain UBS accounts maintained by US clients in Switzerland. UBS was ordered to deliver to the Federal Tax Administration information on accounts that were defined in detail in the treaty agreed between Switzerland and the US. In addition, the bank was required to encourage the US clients concerned in writing to make use of an IRS voluntary disclosure program. Many UBS clients took advantage of this opportunity and have now rectified their tax situations.

Review of events

As of the second half of 2007, a US law firm specializing in this area was mandated to perform an independent investigation of the allegations made by the DoJ and the SEC. This investigation was conducted in continuous consultation with the authorities concerned. This investigation turned out to be the most expensive and comprehensive investigation that UBS had ever commissioned. It examined all potentially relevant aspects of UBS's US cross-border wealth management business with US clients. The SFBC, which was informed about this investigation, carried out its own, independent investigation into these matters.

In conclusion, the following shortcomings had led to the problems with the US authorities:

- *Lack of a comprehensive and continuous risk analysis:* From the year 2000 onwards, UBS had increasingly identified the risks associated with the US cross-border wealth management business, both in connection with the implementation of the QI Agreement and with compliance with the SEC Restrictions. However, with few exceptions the two issues were addressed separately when assessing the risks and taking corresponding measures. The risks resulting from the concurrent operation of both an onshore and an offshore business were not sufficiently appreciated. The consequences of different authorities proceeding jointly in the enforcement of their respective regulations, and the increased regulatory risk profile of UBS due to its US operations, were not adequately assessed or appreciated from an overall, comprehensive perspective. For far too long, too much reliance was placed on

the fact that historically the SEC had not vigorously enforced the SEC Restrictions with respect to the cross-border service of private clients. In addition, UBS failed to implement adequate measures in a timely manner in response to the consequences resulting from the increasing focus that the US authorities placed on the enforcement of their tax regulations, and those resulting from the growing domestic political pressures in the US.

- *Hesitant and incomplete implementation of measures taken:* As the risks, at least in an isolated manner, had been largely recognized, the highest levels of management of UBS had decided to take appropriate measures in order to ensure compliance with the applicable US laws. However, there was repeatedly a lack of sufficient speed and thoroughness when these measures had to be implemented. Such was the case, for example, with the adjustment of the business model in 2002, with the formation of UBS SFA AG, and likewise with the implementation of measures that had been decided upon following the investigation of the whistle blowing by Bradley Birkenfeld. The focus of line management was on the acquisition of new business; insufficient attention was placed on the management of the risks that were simultaneously incurred. Repeatedly, measures that had been decided were enforced only hesitantly and incompletely.
- *Deficiencies in implementation of and compliance with the QI Agreement:* UBS made enormous efforts to implement the QI Agreement, and implemented it in a correct manner to a large extent. However, the client advisors in the US cross-border wealth management business were given too much discretion in their interactions with US clients, and controls were insufficient. This enabled some of the client advisors in a number of cases to assist their clients in efforts to circumvent restrictions relating to the holding of US securities.
- *Insufficient compliance culture and lack of controls:* Full compliance with the complex regulatory framework governing the cross-border wealth management business with clients residing in the US was generally not adequately addressed by UBS. The business was, for example, not effectively monitored and the failures of the employees involved were not consistently detected and corrected. There were also shortcomings in training and guidance, and in the structuring of incentives. The internal guidelines were imprecise and the expectations with regard to compliance therein were not communicated with the required sense of urgency. This allowed client advisors to gain the impression that a certain degree of non-compliance would be tolerated by line managers, which in part turned out to be the case.

On 23 May 2008, the SFBC opened its own investigation into UBS. This investigation resulted in a 161-page "Report by the SFBC on the Implementation of the Qualified Intermediary Agreement and on Cross-Border Services of UBS in the USA (SFBC Cross-Border Report)". The results and materials from the UBS-commissioned investigation were made available to the SFBC, which further examined the events on its own and commissioned an independent investigator to look into certain issues.

The SFBC noted that UBS had taken great efforts to implement the QI Agreement, and that in most respects it had been correctly implemented, but that weaknesses existed in certain areas. These included inadequacies in the monitoring process, on the one hand, and, on the other, generally insufficient enforcement of compliance with the applicable contractual and statutory provisions – both in the area of the QI Agreement and that of the SEC Restrictions. The fact that the employees responsible for the US cross-border business had been granted too much freedom and that their activities had not been sufficiently monitored was identified by the SFBC as a core problem. Another contributing factor was the introduction of a remuneration model which emphasized the criterion of an increase in new client money – an objective in tension with full compliance with US regulations and the terms of QI Agreement.

The SFBC therefore noted that UBS, when implementing its obligations under the QI Agreement and as a consequence of partially insufficient compliance with the SEC Restrictions, took incalculable legal and reputational risks and that by so doing it had infringed on the principles of both proper business management and of proper organization as set forth in the Banking Act. The fit and proper status under the Banking Act of the former members of the corporate bodies, however, was not put in question. The SFBC ordered UBS to adequately address, limit and supervise the legal and reputational risks resulting from its entire cross-border wealth management business, and further ordered that the measures taken had to be the subject of a control by an independent audit firm.

UBS accepts the assessment that emerged from the SFBC investigation and has accepted the measures imposed by the SFBC in its order dated 21 December 2008. Accordingly, it has decided to take a series of measures for the purpose of ensuring that the problems in the cross-border wealth management business do not recur:

- *Exit from the US cross-border business and comprehensive framework of instructions and controls regarding business relationships affecting the US:* UBS has completed its exit from the cross-border wealth management business with US clients, introduced new processes and monitoring systems, and adjusted the provision of certain services so as to ensure that the bank consistently complies with US law with respect to all transactions with clients with a link to the US.

Over a period of one year, a US law firm, acting as an “independent consultant”, with the assistance of the auditing company KPMG, has continuously reviewed the implementation of these measures. This law firm recently confirmed, in a comprehensive report to the SEC and the DoJ, that the measures had been successfully implemented.

- *Improved internal instructions and enhanced controls of the cross-border wealth management business:* Within the framework of extensive projects, UBS has identified all risks in the cross-border businesses of all its business divisions, including the global wealth management business and the Investment Bank, and adopted numerous far-reaching measures to adequately monitor these risks.

In the cross-border wealth management business of the business division Wealth Management & Swiss Bank, new instructions have been issued, and independent monitoring

procedures introduced with regard to the rules of providing advisory and asset management services, restrictions regarding the distribution of certain products and related information, disclosure and notification duties as well as to rules regarding investment restrictions for clients from certain countries. Moreover, there has been a fundamental revision of the guidelines and monitoring measures for business relationships with domiciliary companies and external asset managers. Finally, UBS performed a fundamental review of its own range of estate and wealth planning instruments: it has subjected the providing of services in this area to new internal guidelines and to strict risk monitoring. In particular, UBS does not offer services in this business sector whenever the client advisor is aware, or has indications, that the client intends to make use of such services for the purpose of avoiding taxes. With these measures in place, UBS is convinced that it will appropriately master and control existing risks and future opportunities in the constantly changing environment of the cross-border wealth management business.

UBS kept FINMA regularly informed about the progress made in implementing these measures. FINMA will mandate an independent auditing company in the fourth quarter of 2010 to review the adequacy and effectiveness of these measures for controlling the legal and reputational risks.

- *Enhanced organization and framework of instructions and controls regarding the implementation of the QI Agreement:*

In order to enhance instruction and control processes with regard to compliance with the QI Agreement, UBS has introduced the functions of a “Group Head US Withholding and QI Compliance” and a “QI Tax Coordinator”. The persons responsible for these functions, supported by additional personnel and additional financial resources, have improved the entire instruction and monitoring framework. Over the last year, the auditing company KPMG has reviewed the implementation of the new measures and recently confirmed the successful completion thereof in a comprehensive report to the DoJ and the IRS.

- *Ensuring the independence of the legal and compliance functions:*

The events that transpired in the US cross-border business have highlighted the importance of maintaining the full independence of the UBS legal and compliance functions. Today, the reporting lines within Legal & Compliance always must take precedence over the information lines to the line functions; dual reporting lines have been abolished. In addition, UBS has assigned the exclusive authority for decisions for remuneration and promotion issues in Legal & Compliance to the UBS General Counsel. Finally, by introducing the function of a head of global compliance with central units, UBS has strengthened significant aspects of global compliance procedures and monitoring.

Part III.A (cf. below page 32 ff.) of this transparency report presents background information on the circumstances that led to the proceedings before the US judicial authorities. The investigations conducted by UBS in connection with the cross-border wealth management business in the US are described in Part III.B (cf. below page 35 ff.). Details on the review conducted by domestic and foreign supervisory authorities follow in Part III.C (cf.

below page 38 ff.) Finally, Part III.D (**cf. below page 43 ff.**) provides information on the measures that UBS implemented to conduct its future cross-border wealth management business in full compliance with applicable domestic and foreign regulations.

Liability issues

On 15 December 2009, the UBS Board of Directors announced that it will not initiate criminal or civil action against the former directors and senior officers of the bank. The public prosecutor of the canton of Zurich had previously communicated that no initial grounds for suspicion had been established that would justify initiating a criminal investigation against any former UBS directors or officers.

The UBS Board made the decision after careful consideration based on reports of a number of law firms that had examined the question of liability, and further based on a comprehensive documentation resulting from the investigations of these matters. Having re-examined all relevant facts, the Board stands by this decision. It is convinced that the decision not to initiate criminal and civil action against former directors and senior officers is based on a correct legal assessment, and is in the best interests of UBS.

It is important to emphasize in this context that the risk control failures in the US mortgage business or insufficient compliance in the US cross-border wealth management business do not automatically result in civil liability on the part of the members of management or of the Board of Directors. Rather, liability of the former directors and senior managers is contingent upon the fulfillment of certain legal requirements. Liability of directors and officers is dependent upon the fulfillment of four conditions: a breach of the duty of care, a loss, a so-called causal link between the breach of duty and the loss, and a personally attributable fault.

In particular, in view of the strict legal requirements of liability claims in Switzerland and weighing all relevant factors, the Board of Directors concludes that filing directors' liability actions is not in the interest of the company, and that the filing of such actions cannot be justified by a reasonable cost/benefit analysis. This conclusion is based on the following considerations:

– *Prospects of success of an action:* Neither the SFBC investigation nor the preliminary investigation by the public prosecutors produced findings to suggest that a successful outcome of a lawsuit was sufficiently likely. UBS itself has commissioned a number of extensive internal and external investigations since 2007. These investigations also did not produce such findings.

Furthermore, the damages that could be recovered by an action against former directors and senior managers would be limited to the personal assets of the defendants concerned and the level of insurance coverage (whereby successful claims for insurance coverage would ultimately result in UBS indirectly financing these insurance payments through increased insurance premiums). It should be noted in this context that a number of former directors and senior managers, who may have been faced with an action, waived claims for or repaid salary and bonus payments in

an amount of more than 70 million francs. The Board of Directors viewed these gestures as an indication that the former directors and officers of the bank had acknowledged at least their moral responsibility, even if they were not to be held liable under the law.

– *The interests of the company:* Based on its duty of care under corporate law, the UBS Board of Directors had not only to assess whether a lawsuit promised a successful outcome, but also whether such a lawsuit would be in the interest of UBS and of its shareholders. This follows from the statutory duties of the board of directors of a stock corporation to safeguard the interests of the company in all its actions and decisions. The UBS Board must therefore also consider whether an action against former directors and senior managers would be in the interests of the company. The Board can and must therefore decide against an action if it concludes that a lawsuit would cause more harm than good to the company.

The Board carried out a cost/benefit analysis that took into account the costs of an action, the amount of management time and attention that would be absorbed by it and the negative publicity effects that such litigation would bring, including a public discussion with negative headlines focusing on the past failings of UBS rather than on the newly organized bank. In the opinion of the Board, the likelihood of success of a lawsuit was not sufficiently high to justify these costs and negative effects.

– *Potential further consequences of an action:* Class-action suits against UBS are already pending in the US in which billions of dollars are claimed. UBS is of the opinion that these claims lack any basis both as regards the facts and the law, and it will vigorously defend its interests in these proceedings. If UBS now brings an action in Switzerland against its former directors and senior managers, under normal US practice this alone could be considered – regardless of whether such an action ultimately succeeds or fails – an admission that they had in fact acted improperly. This would severely impede UBS's defense in these proceedings.

In addition, one would have to expect "free riders" of all kinds to join in such an action in Switzerland. All this would have unforeseeable negative implications for UBS and, given the enormous significance of business with the US and other foreign clients throughout its history, for the entire Swiss banking industry as a whole.

Finally, an action could produce a situation in which former directors and senior managers attempt to assign blame to and litigate against one another or even seek to draw present directors and managers of UBS into such proceedings. This would serve neither the interests of UBS nor those of its shareholders.

– *Impact on shareholders:* Ultimately, the costs of an action initiated by the company – or of pending proceedings in the US – would have to be borne by the shareholders as the owners of UBS. Therefore, an action would have direct consequences for each and every shareholder. The fact that the largest shareholders of UBS have never requested the company to initiate an action confirms the decision by the Board of Directors.

- *Looking to the future:* If the current UBS Board were to initiate an action against former directors and senior managers, it could be accused of throwing good money after bad. In addition, due to the above-mentioned side effects, UBS and its employees could be distracted for years from their day-to-day operations, while the confidence of clients and of the financial community in general might suffer. The Board of Directors feels that this would be irresponsible.

Having considered all the above factors and after weighing all arguments, the Board of Directors decided not to take further legal action against its former directors and senior managers. For all of the above reasons the Board is also against any initiative by third parties to file actions against former directors and senior managers or to even pursue actions at the company's expense.

Part IV.A (cf. below page 51 ff.) of this transparency report explains in detail the questions which UBS has examined in connection with potential directors' liability actions under corporate law. Part IV.B (cf. below page 56 f.) describes the investigations carried out by UBS and the public authorities in the field of criminal law. Part IV.C (cf. below page 58) explains in detail why the Board of Directors decided to refrain from pursuing civil and criminal action against former directors and senior managers.

Where does UBS stand today?

The various analyses, opinions and reports summarized in this transparency report show a number of shortcomings in different areas of the company which together contributed to the problems UBS has faced. This suggests that cultural factors have supported the occurrence of these unfortunate developments. As a result of the internal and external investigations, the Board of Directors concluded that not only technical and financial market specific, but also cultural factors contributed to the problems of UBS. Acting on this conclusion, the new management of UBS is endeavoring to create a more sustainable corporate culture within UBS. At the same time, it must be emphasized that throughout the financial market crisis, that is, from mid-2007 through the beginning of 2009, many UBS employees and managers remained unflinchingly committed to maintaining daily business operations. Today, UBS is of the opinion that it has learned its lessons from the crisis and that it has made significant progress in recent months. UBS is the largest bank in Switzerland and a worldwide leader in wealth management. It has stabilized financially and is well capitalized with a Tier I capital ratio of 16.4 percent as of the end of June 2010. UBS has also been recording profits again since the fourth quarter of 2009. In the first half-year of 2010, pre-tax consolidated profits amounted to 5.4 billion francs. The bank's risks, measured in terms of its risk-weighted assets, and its balance sheet total have been reduced by nearly 50 percent since mid-2007.

Since the outbreak of the financial market crisis, the Board of Directors and the Group Executive Board have undergone a comprehensive process of renewal, in terms of both the composition of their membership and their functional operations. The governance structures needed for steering the bank's busi-

ness in a consistent manner and for effective monitoring have been put in place.

The new Board of Directors and senior managers place the utmost importance on UBS and its employees being perceived as trustworthy partners. For this reason, it has given intense attention and consideration to the priorities of the business, its structure and processes, and the new corporate culture. The paramount objective was to create a new UBS capable of sustainable high performance.

The following cornerstones indicate the priorities that UBS will be pursuing in its various business divisions:

- *Wealth Management:* UBS plans to further strengthen its position in wealth management for private clients. In doing this, it is of the utmost importance that the rules and regulations of the individual countries be respected at all times – and without exception. In this regard, UBS has issued internal guidelines and instructions that are among the most stringent in the industry and which set new industry standards.
- *Investment Bank:* The business model and monitoring structures of the UBS Investment Bank have undergone a comprehensive revision. Its individual business units have now been closely coordinated with each other and are closely monitored. Its business focus is clearly directed toward advisory and client services, while the level of proprietary trading has, accordingly, been drastically reduced.
- *Asset Management:* In the area of institutional asset management, UBS has carried out various initiatives for ensuring that a consistently high level of investment performance is achieved. Internal cooperation with the bank's wealth management divisions and with the Investment Bank has been intensified and institutionalized to provide clients with a wide offering and a maximum of added value.
- *Regions:* In the domestic Swiss market, UBS intends to maintain and further strengthen its number one position. As the main capital market in the world the US will remain pivotal for the investment banking activities of UBS. Asia is crucial as a growth market for all business divisions.

With regard to the company's corporate culture, three main strategic principles have been defined to which all employees are expected to conform: reputation, integration and execution. These principles are supplemented by the core values of truth, clarity and performance. At the beginning of 2010, UBS introduced a new, comprehensive code of conduct and ethics. The principles and standards described in the code make it the personal responsibility and duty of every employee to act in a compliant and ethically correct manner.

Switzerland plays a special role for UBS because it has its roots here and, with respect to its business divisions and client segments, the bank is firmly linked to this country. UBS headquarters are located in Switzerland and over a third of its entire personnel, that is over 23,000 employees, are located here. UBS is one of the largest listed companies in the country. Roughly 2.5 million private Swiss individuals and some 135,000 Swiss companies – that is, nearly every second enterprise in the country – have a business relationship with UBS. UBS also plays an important role for Switzerland both as an employer and as a

provider of professional training in banking: in 2010, nearly 700 new university graduates, over 800 interns and some 300 trainees have already been hired.

UBS plans to strengthen its relationship with all Swiss interest groups, to encourage dialogue and to communicate more actively. It hopes to create understanding for its own positions and actions and, at the same time, understand the positions of others. The fact that UBS brings its own interests to discussions

about Switzerland's future as a financial center is a part of the responsibility it bears toward its clients, its shareholders and its employees all around the world. At the same time UBS recognizes and takes into account its relevance for the stability of the Swiss financial system.

UBS is convinced that it has overcome the crisis. Where UBS stands now and its priorities for the future are described in Part V (**cf. below page 59 ff.**) of this transparency report.

II. The financial market crisis

A. What led to UBS's losses during the financial market crisis?

UBS had to write down more than 50 billion Swiss francs between the third quarter of 2007 and the fourth quarter of 2009. The following explains what led to these write-downs and the related UBS losses.

1. Financial products in the US real estate market

The turbulence in the US real estate market in the middle of 2007 came as a surprise both to UBS and to many other financial institutions, particularly in terms of its speed and intensity. In the preceding years, the real estate market in the US had expanded rapidly. What factors led to this rapid surge in the market and its subsequent dramatic collapse?

This growth was favored by many years of consistently low base interest rates set by the Federal Reserve (FED), combined with low inflation. Many market participants believed that inflation-free growth would continue in the future and that, in consequence, a continued increase in real estate values was guaranteed. The US government fostered these developments with a political program that promoted home ownership for lower income groups.

A market for mortgage loans had already developed during the 1930s: it was the business of the Federal National Mortgage Association (FNMA), founded in 1938, supported by the US government and known as Fannie Mae, to acquire mortgages from lending banks and to place them on the market. Beginning in 1979, the same line of business was pursued by the Federal Home Loan Mortgage Corporation (FHLMC), known as Freddie Mac. Fannie Mae and Freddie Mac were leaders in this business. Certain market participants put the creditworthiness of their bonds on par with US government bonds. Fannie Mae and Freddie Mac had a de facto government guarantee on their liabilities. These two institutions secured by far the largest share of private residential mortgages by means of guarantees, financed them directly or indirectly, and even assumed them in their entirety.

The securitization of risks associated with the US real estate business expanded in the middle of the 1980s, and this business was increasingly pursued by other financial institutions. The securitization business of banks in the US real estate sector was continuously expanded at the beginning of this millennium, thus contributing significantly to the financing of the market's growth.

Background

Securitization in the real estate sector results in lending banks not keeping their individual loans on the balance sheet until maturity; instead the lending bank sells the loans and the resulting risks to specialized financial institutions that bundle these loans and transfers them to third-party investors.

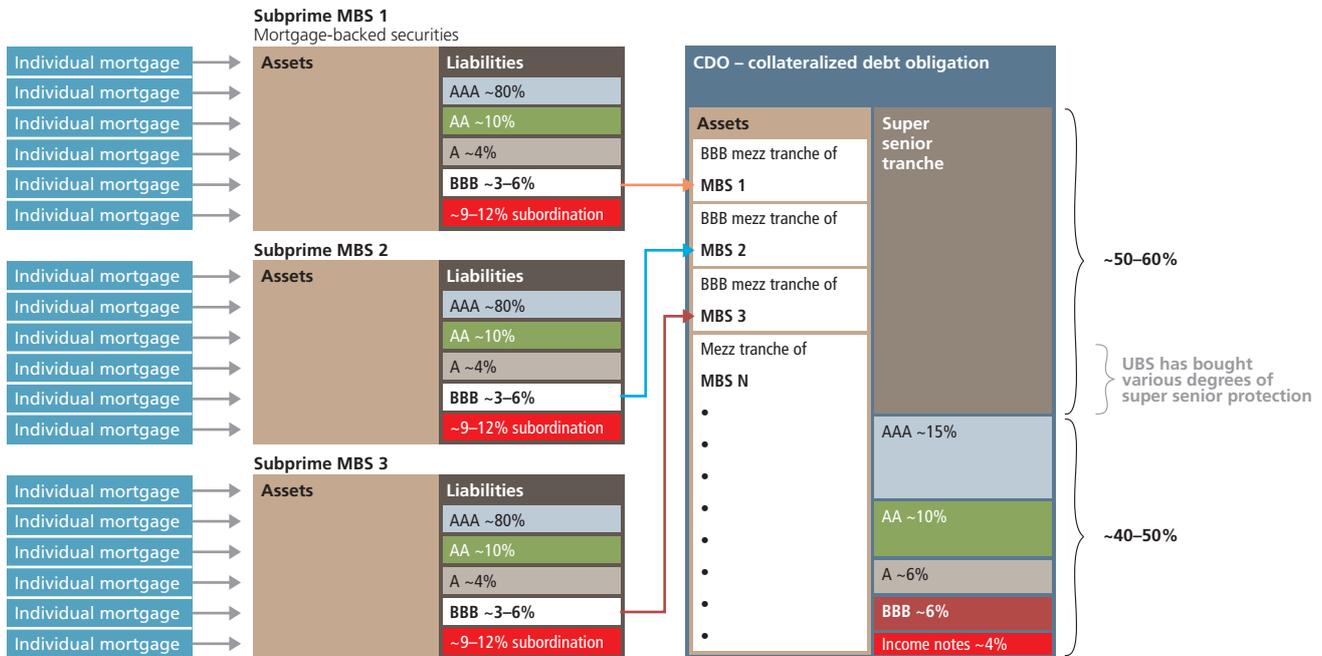
Over time banks securitized mortgages by transferring assets into special purpose vehicles (SPVs), generally with no financial institution guaranteeing the payment of either principal or interest. The return on investment for the investor was therefore exclusively dependent on the performance of the mortgages that were bundled in the respective SPV. Bonds issued by the SPVs that were linked to bundled residential mortgages were called mortgage-backed securities (MBSs). Other investment instruments issued by SPVs based on other assets such as credit card claims or student loans were generally called asset-backed securities (ABSs).

The further evolution of the business of securitization resulted in the creation of complex structured products which included – depending on the risk appetite of the investors – lower- or higher-risk MBS and ABS. This was achieved, among other means, by issuing different types of bonds, all linked to a particular bundle of mortgage loans. Depending on the tranches of bonds, the payment terms varied. If a debtor was no longer able to honor its mortgage loan commitments, the first investors to be hit were those who had invested in the tranche of bonds that carried the lowest credit rating and the highest risk. The high risk of these investments was compensated by the promise of a high return. Investors in tranches of higher quality considered their investments safe, as they were ranked first for the distribution of cash flows and were therefore to be the last to suffer potential losses. Even greater complexity resulted from the bundling of tranches of bonds of the same risk category into an SPV, on which that SPV then issued additional bonds in several tranches and various risk categories. These instruments are known as collateralized debt obligations (CDOs). Within a CDO, the tranche with the lowest risk was referred to as “super senior” (cf. graph page 17.).

The business with complex structured products based on the risks of the US real estate market experienced a veritable boom, beginning in 2005. Because the loan interest rates in the US had remained at a historically low level since the turn of the century, persons with relatively low income were now able to afford to purchase residential property. This led to an increasing demand for mortgages. It was generally expected that the growth in the country's economy would lead to a constant increase in real estate prices at constantly low lending rates. Many banks were prepared to grant loans and to constantly lower their requirements with regard to the credit rating of the underlying assets, the solvency of the debtors, or the quality of the credit documentation. In the expectation of constantly low interest rates and increasing real estate prices, they assumed that losses would remain under control. Indeed, the lending banks had little incentive to perform strict credit checks on their mortgage borrowers, since the risks associated with the mortgage loans were passed on to third parties, who bundled them into MBSs that they then sold to investors.

Super senior CDOs

A super senior CDO is the most senior piece of a collateralized debt obligation's capital structure, which is the least likely part to default (second level securitization after MBS/RMBS). In case of default, super-senior CDO tranches rank higher than triple-A-rated tranches of the same capital structure. Super senior CDOs only paid little return given that they were perceived as almost risk-free.



Note: While the junior notes behind the BBB mezzanine tranche are typically very thin, the total credit support for the mezzanine tranche is typically in the range of 9 to 12 percent in form of income notes, excess spread and overcollateralization.

Source: SFBC UBS Subprime Report, page 5

Background

The possibility for a debtor in the USA to take up a mortgage loan which is exclusively secured by the underlying real estate (so-called "non-recourse loans") without assuming personal liability facilitated this development. An increasing number of mortgage loans were granted to debtors who had neither a regular income nor material assets at their disposal. The respective loans – known as subprime loans – showed by far the largest growth during the years prior to the financial market crisis.

These factors led to a spiral of rising house prices, larger mortgages, more complicated methods of securitization and stronger investor demand for MBS products. Although most market participants recognized that the credit rating of the underlying receivables was declining, it was widely assumed, until the summer of 2007, that any correction in the real estate market would be only minor.

Similar methods of securitization were also employed in other areas, where large pools of underlying claims were bundled and could be passed on to investors. This allowed an increasing number of leasing commitments, credit card debts, student loans, etc. to be refinanced.

2. UBS's exposure to the US real estate market

UBS and other financial institutions early recognized the potential offered by the US housing market. By bundling, securitizing and reselling US mortgage receivables to interested investors in the market, banks were able to remove them from their balance sheets. Investors in turn had the opportunity to invest in various financial products derived from real assets, each with a different risk profile. The returns on such financial products were also frequently more attractive than those on investments with a comparable rating, such as government bonds.

Over time, in addition to top-quality mortgages, UBS also began to bundle, securitize and resell mortgages tied to lower solvency borrowers. Investment products derived from mortgages granted to prime or near prime borrowers were designated as "prime mortgages", those granted to borrowers with good creditworthiness but partially incomplete credit documentation were designated "Alt-A", while those granted to poorly rated borrowers or with mortgages above the normal lending limits were referred to in the jargon as "subprime" mortgages. The recent global financial market crisis had its origin in the subprime sector, but then extended to the entire US housing market, and finally to other investments with US borrowers

(students, lessees, credit card holders, etc.). A large share of the losses that UBS suffered during the financial market crisis were related to complex structured financial products based on the US mortgage market.

Traditionally, each UBS business unit had been responsible for managing its own risks, in keeping with the instructions provided by the Group Executive Board and the business unit management. In other words, when a business unit made an investment, it was also required to appropriately manage and limit its risks. In terms of risk management, business units active in securities trading, or their traders, were responsible for determining the value of the positions they held on a daily basis. The Business Unit Control (BUC) periodically performed independent checks on these valuations, using precisely defined criteria. Where subprime securities were concerned, a great deal of confidence was placed in the security ratings furnished by credit rating agencies.

Background

Credit rating agencies such as Standard & Poor's classify investment products according to creditworthiness into categories ranging between AAA (highest creditworthiness) and D (bankrupt). The intermediate rating levels (AA+, AA, AA-, A, BBB, BB, B, etc.) provide information on the presumed risk of default. Investments with a creditworthiness of BBB- or higher are designated as high-quality investment products ("investment grade"), and investments with a creditworthiness of BB+ or less as speculative securities ("speculative grade").

Other credit rating agencies, such as Moody's, and Fitch, use comparable ratings. In the interests of simplicity, this report only refers to the rating levels used by Standard & Poor's.

An important risk management tool, and common practice at that time, was the use of statistical models to calculate the probability of future losses for a given position and thus also the required valuation adjustment for that position, based on historic market data. Most of these risk models employed market data from the preceding five-year period. The stable market environment in the years prior to 2007 caused these models to be based on low levels of market volatility. By relying only on data from the recent past, models were unable to predict significant market fluctuations in the future. In retrospect, models designed in this way were far too optimistic and ultimately led to an underestimation of the risks and the size of the losses that were later incurred.

Further, the situation was exacerbated by the fact that, prior to the financial market crisis, UBS had no uniform system for valuing the risks of US mortgage-based securities. This meant that different business units valued the risks inherent in same positions differently. Balance sheet limits that would have limited the amounts invested in specific investment categories, such as subprime securities, were also lacking. Before the crisis, UBS and many other major banks felt that such nominal balance sheet limits were not suitable for the managing of investment risks.

In summary, it emerged that, prior to 2007, UBS Investment Bank had placed too much confidence in the qualitative, consis-

tently positive assessments provided by the credit rating agencies and in quantitative risk models.

At the same time, until the outbreak of the crisis the supervisory authorities and controlling bodies confirmed to UBS that its risk management system was adequate: UBS's statutory auditor, Ernst & Young AG, raised no objections in its annual examinations that would have suggested that its subprime holdings had not been properly valued in 2006 and 2007, or that UBS's reporting system was inappropriate for the business risks it had to monitor. The competent supervisory authorities, in particular the SFBC and US Federal Reserve, also assumed that UBS was a well-managed bank with adequate risk control mechanisms.

3. Outbreak of the crisis

Until the beginning of August 2007, the senior management of UBS was of the opinion that, in the framework of its trading activities with securities from the US real estate market, investments had been made in high-quality products that would not suffer significant losses even if there was a drastic cooling of the market. UBS based this belief, in particular, on the positive ratings assigned to its financial products by the rating agencies. In addition, many of the investment products included special credit insurance (credit default swaps or "CDSs") which was intended to cover any cases of default.

UBS Investment Bank became aware of the problems connected with the salability (and therefore with the valuation) of high-quality US investments at the end of July 2007, in the course of preparing the consolidated financial statements for the second quarter of 2007. The Chairman's Office of the Board of Directors and the Group Executive Board were informed of the situation on 6 August 2007. The public was informed shortly afterwards: in addition to the announcement of a consolidated profit of 5.6 billion francs, UBS on 14 August 2007 also informed shareholders and the public for the first time of problems related to the imminent crisis.

"Markets are, however, highly volatile at present, making the forecasting of future developments more difficult than usual. Our trading results could be seriously negatively affected if the current turbulent conditions continue through to the end of the third quarter."

UBS press release of 14 August 2007

The course of events mentioned in August as a possibility became actual fact during the third quarter. On the first trading day following the close of the third quarter, UBS announced a write-down on the order of 4 billion francs:

"UBS will realize substantial losses in the third quarter (...) in its investment bank, mainly on mortgage-backed securities in the US subprime residential real estate market (...) These write-downs are primarily for a) old liabilities from the Dillon Read Capital Management unit, which has in the meantime been dissolved, and b) positions taken by the investment bank in its mortgage-backed securities trading (MBS)."

UBS press release of 1 October 2007

4. Measures taken by UBS to strengthen its capital base

Severe turbulence in the US mortgage market and in global financial markets subsequently made it necessary, however, to take additional write-downs and to announce further losses. Even investment products with a triple-A rating, that is, products considered to carry virtually no default risk over the next one-year period, proved not to be safe against depreciation in value under the market environment prevailing at that time. As soon as it became clear that the problems related to the US market would be long-term in nature, and not just temporary, UBS quickly implemented a recapitalization plan. Because of this swift reaction by the bank's senior management at the time, UBS succeeded in maintaining robust capitalization and liquidity levels through to the fall of 2008:

- On 10 December 2007, UBS announced approximately 10 billion US dollars in additional write-downs. At the same time, the bank announced that it had taken measures to increase its capital base by 19.4 billion francs. These measures included the issuing of 13 billion francs in new equity that was placed with a Singapore government sovereign wealth fund and an investor in the Middle East. In addition, treasury shares were sold and a stock dividend, rather than a cash dividend, was paid for financial year 2007. The amount of capital raised through these measures was higher than the write-downs that had been announced up to that time for positions deriving from the US housing market.
- Additional write-downs in the first half of 2008 made another capital increase necessary. On 1 April 2008 UBS announced a public capital increase. This was completed in June 2008 and raised approximately 15 billion francs in additional funds for the bank.

However, the crisis worsened. On 15 September 2008, the US investment bank Lehman Brothers filed for insolvency with the competent courts. This was the first insolvency of a large financial institution in the crisis. The result of this event was that the granting of short-term credits in the inter-bank market came to a gradual standstill, due to a loss of confidence. Central banks around the world were called upon to provide massive injections of liquidity in order to ensure that money continued to flow between banks. Various governments, including those of the US, Great Britain and Germany, ordered state capital contributions for individual banks for which they were directly responsible. Switzerland also provided funds to the banking system. UBS and the SNB agreed that UBS would sell a portion of its holdings in US and other securities to a special purpose vehicle to be established by the SNB under the name "SNB StabFund". Securities with a total value of 39.6 billion dollars were transferred to the special purpose vehicle between fall 2008 and spring 2009. In order to enable the bank to meet its equity requirements for these transactions, the Swiss Confederation, on 15 October 2008, subscribed for UBS mandatory convertible bonds in the amount of 6 billion francs.

Background

In the summer of 2009, the Swiss Confederation sold the UBS shares it had acquired through the capital injection at a profit of approximately 1.2 billion francs. By the end of June 2010, the SNB's total exposure had fallen to 19.2 billion dollars, and in the first semester of 2010, the SNB StabFund has contributed profits of 1.3 billion francs to the earnings of the SNB.

By the end of 2009, the total cumulative amount of UBS's write-downs exceeded 50 billion francs. Total write-downs taken by banks worldwide, as of April 2010, are estimated at approximately 2,300 billion dollars.

B. How did UBS review the crisis?

1. UBS investigations

In the fall of 2007, at the suggestion of the SFBC, Peter Kurer, at the time the general counsel of UBS, commissioned an extensive internal investigation into the causes of the financial market crisis and its effects on UBS.

Background

The crisis was still in its beginning stages at this point in time. The most dramatic events would not occur until a year later, in September 2008, when the US investment bank Lehman Brothers filed for bankruptcy. UBS estimates that in October 2008 a total of 28 banks worldwide had to accept a total of USD 264 billion in government aid (in October 2008 UBS, as mentioned, received a financial injection from the Swiss Confederation in the amount of CHF 6 billion).

Currently, various foreign governments still hold investments, some of which are considerable, in the banks they stabilized (Great Britain, for example, at the end of 2009 with GBP 89 billion, that is, approx. CHF 133 billion).

This investigation was conducted by a large internal team, and required several thousand working hours. The confidential report (UBS Report to the SFBC) prepared during this investigation and

signed by the Group General Counsel comprised some 700 pages and was submitted to the SFBC on 4 April 2008. In order to also inform shareholders and the public as to the reasons for the write-downs, UBS obtained approval from the SFBC to publish a roughly 50-page English summary of the report (UBS Shareholder Report), which was issued on 21 April 2008.

The primary objective of the investigation was to draw lessons from the crisis for the future:

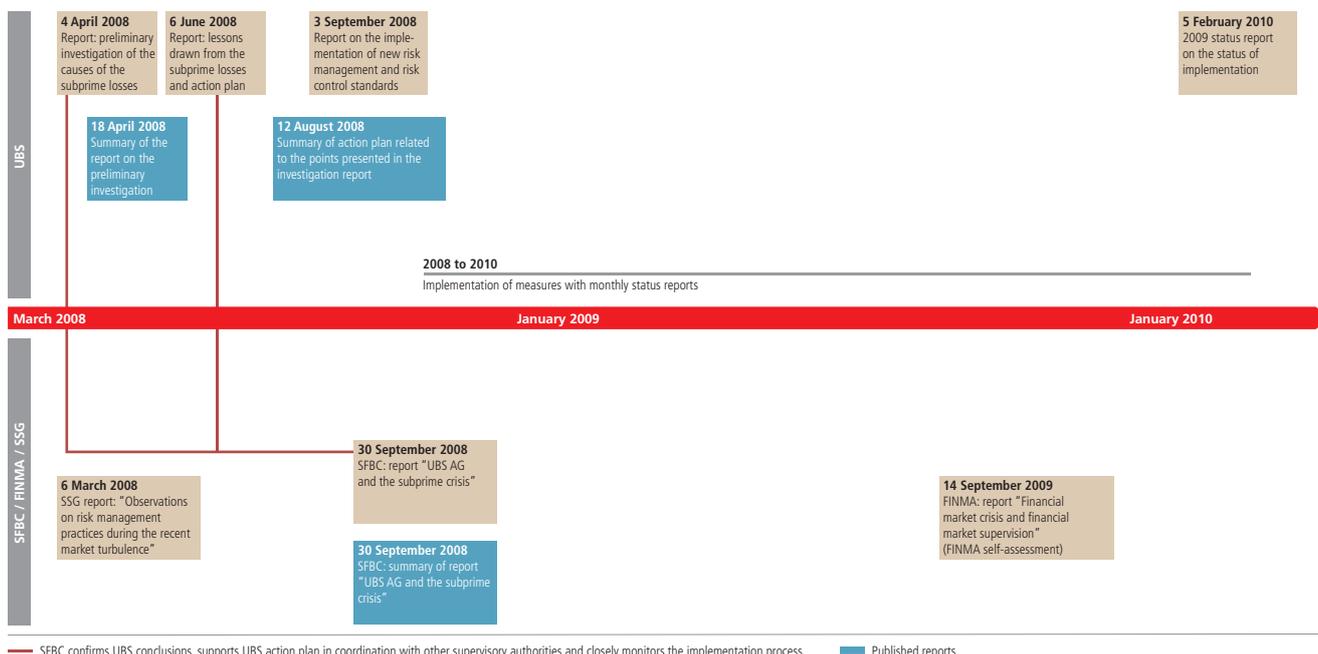
- The lessons drawn by UBS and the measures planned in order to prevent further losses were subsequently described in detail in the UBS internal report "UBS's Write-downs Arising from the Market Dislocation: Lessons Learned and Remediation", dated 6 June 2008.

Based on its own investigation into the subprime crisis (cf. below page 26), the SFBC considered that the proposed action plan was adequate. This action plan included wide-ranging measures in the areas of corporate governance, risk management, risk control, financial functions, financing and balance sheet management, compensation and strategy. All measures have in the meantime either been implemented or the implementation is in progress.

In addition to UBS, the SFBC also performed an investigation of the crisis and of UBS's role in it. The chart shows the different investigations that were conducted. More detailed information on the SFBC investigations is provided below (cf. below page 24 f.).

Chronology of reports and events – subprime

UBS analyzed the root causes, drew the lessons and took action



2. Business areas affected by losses

The reports prepared by UBS showed, inter alia, which business areas had been affected in which manner and to what extent by the crisis in the US real estate market. Investments in financial products linked to the US housing market were made by a number of business units of the UBS Investment Bank into the summer of 2007. With the outbreak of the financial market crisis in the summer of 2007, the market for these financial products collapsed and they could either no longer be sold, or sold only at a considerable loss. As mentioned, this meant that corresponding positions had to be valued much lower than earlier assessments. This made significant write-downs necessary in the Investment Bank area, which ultimately led to the losses UBS suffered.

a) Dillon Read Capital Management

In June 2005, UBS announced that a portion of its fixed interest investment business was being transferred to a subsidiary with the name Dillon Read Capital Management (DRCM). DRCM was intended as an investment platform that would develop alternative investment vehicles, particularly in the area of the US mortgage market, both for clients and for UBS's own accounts.

Background

UBS's spin-off of DRCM was specifically intended to appeal to investors with a high risk appetite. DRCM deliberately invested in subprime investments, that is, lower-quality products based on the US mortgage market that rating agencies generally did not classify as high-quality investment products ("investment grade").

In its quarterly financial statements of 31 March 2007, DRCM stated that some of the securities it held had to be written off due to a lack of liquidity; the corresponding losses could only in part be compensated by the available hedging transactions. Subsequently, UBS wrote down 150 million francs on DRCM's assets in its consolidated financial statements for the first quarter of 2007. On 3 May 2007, UBS also announced that it would be closing DRCM and reintegrating the investment platform's trading book into the Investment Bank. In retrospect the reintegration of DRCM into UBS Investment Bank in the second quarter of 2007 tied up a large amount of resources that were then not available for other purposes at the outbreak of the financial market crisis.

b) The Investment Bank

With the creation of the DRCM investment platform, John Costas, then head of the Investment Bank division, and Mike Hutchins, then head of the Fixed Income, Rates and Currencies area (fixed income products and foreign currencies), moved to DRCM. In the fall of 2005, Huw Jenkins, the successor of John Costas, commissioned a study to analyze how UBS Investment Bank should best position its business in the future. The study concluded that UBS Investment Bank should continue to promote its fixed interest investments – even after the creation of DRCM – so as to become one of the leading banks in this sector worldwide.

In the follow-up to this study, the Investment Bank continued to expand its business, also in the US mortgage market. This expansion took place in parallel to DRCM's business. The

investments in this market were made by a number of different business units within the Investment Bank.

(1) Fixed income: CDO desk

The majority of the losses suffered by the UBS group in connection with the US mortgage market originated with the Investment Bank's CDO desk.

Background

CDOs are complex structured financial products based on a pool of assets in the same category. Prior to the financial market crisis, the underlying assets were primarily US mortgage loans, as well as loans to US university students, credit card receivables, leasing receivables and the like.

In simple terms, in order to create a CDO, a pool of receivables in the same category is assembled and then divided into a number of tranches with differing credit ratings. If losses are incurred by a pool of receivables, these are borne first by the investment products in the tranche with the lowest credit rating. Although these products carry the greatest risk, they also promise the highest return.

High-quality investment products were the last to bear these losses. The lowest level of risk was offered by securities with a AAA rating and an even higher rated tranche referred to as "super senior".

Unlike DRCM, the CDO desk did not invest in CDOs or in the securities underlying the CDOs for its own account only. This business unit was engaged in origination and underwriting, that is, in the business of purchasing, bundling and reselling investment products. The only tranches that UBS normally held for its own account were super senior tranches, which had the highest credit rating and were considered virtually risk-free.

The first step in the CDO desk's origination and underwriting business was the purchase of the underlying securities, such as MBSs, which were then held in what was referred to as a "CDO warehouse" until such time as they were resold to investors. The receivables were reported as assets on UBS's balance sheet until the time they were resold. Once a tranche had been completed in the warehouse, the receivables and the underlying credit risks were transferred to a special purpose vehicle (CDO special purpose vehicle) and then sold to investors. When this occurred, the MBSs in the warehouse were removed from the UBS balance sheet, while the resulting sales revenues were booked as profit.

The business of structuring, bundling and reselling US mortgage securities grew significantly in 2005 and 2006 and was highly profitable.

During the financial market crisis, however, the positions that had been prepared in the warehouse for resale suddenly became unsellable, and the CDO desk was left holding them. With the collapse of the US mortgage market, it further became apparent that, contrary to all expectations, the super senior positions held by the bank for its own account had also suffered losses. As a matter of fact, in 2007, UBS's largest losses occurred from these super senior positions. In addition, products that were purchased to hedge some of the super senior positions only covered a few percentage points of the losses incurred.

(2) Foreign exchange/cash collateral trading

The Investment Bank also had a business unit with the name Foreign Exchange/Cash Collateral Trading (FX/CCT). This unit was responsible for ensuring liquidity for the entire group, that is, not for the Investment Bank alone.

FX/CCT invested in products considered at the time to be of low risk and highly liquid, that is, products that could be sold quickly on the market. As part of its business activities, FX/CCT in 2003 began assembling a portfolio that consisted increasingly of investment products linked to receivables from the US mortgage business.

Background

This took place following UBS's decision at the end of 2002 to reduce its investment in Japanese government securities, which were considered too risky. As mentioned, US mortgage products were considered safe market instruments at the time. The confidence placed in these products was principally based on the high ratings (AAA or AA) assigned to them by the rating agencies.

In the end, FX/CCT losses represented approximately 10 percent of the total subprime losses incurred in 2007.

(3) Other Investment Bank business units

In addition to the business units indicated above, losses also came from other units of the UBS Investment Bank (ABS/MBS desk, Securitized Product Group Proprietary Trading Desk, and Credit Fixed Income). These units had also invested in investment products that subsequently retained little or none of their value.

3. How was it possible for the losses to occur?

The internal UBS reports mentioned above provide detailed information on how UBS's losses developed during the financial market crisis up to the end of 2007, and the reasons for these losses. The UBS Report to the SFBC and the UBS Shareholder Report identify nine fundamental causes for UBS's losses. As part of the UBS internal review, each cause was assigned to one of the categories of "strategy", "corporate governance", "risk management", "risk control and finance", "funding and balance sheet management", and "compensation", and addressed using a variety of measures (cf. below page 26 ff.).

As discussed below (cf. below page 24), the SFBC concluded that UBS had correctly and comprehensively identified the following reasons for the financial market crisis and its balance sheet effects.

- *Growth strategy:* In the summer of 2005, UBS spun off a significant portion of its activities in fixed income investment products into its subsidiary DRCM (cf. above page 21). At the end of 2005, a decision was made to simultaneously develop a growth strategy in this sector within the Investment Bank. The objective was to become one of the top banks in the world in this sector and to catch up with the competition. First, however, the required resources had to be assembled, as many specialists had since moved to DRCM. The growth strategy in the fixed income sector was also intended to fill

the gap that had been created by the spinning off of part of the bank's business to DRCM.

In retrospect, the growth strategy was not planned systematically enough and it was implemented without sufficient monitoring.

- *Different business units performing the same business activities in the group:* DRCM was an independently managed investment platform within the UBS group. As such it directly invested in products linked to the US mortgage market. There were a number of other business units in the Investment Bank that also invested in US investment products or carried out the structuring and resale of such products (cf. below page 21).

Since the growth strategy in the fixed income business was not centrally planned and managed, the activities of the various business units within the Investment Bank were not sufficiently coordinated.

- *No balance sheet limits:* Prior to the financial market crisis, the bank did not set balance sheet limits. In combination with the other reasons discussed here, this allowed the accumulation of massive holdings of US mortgage securities, which had devastating consequences as this business began to collapse.
- *Favorable refinancing rates:* Until the outbreak of the financial market crisis, the interest rates for short-term funding were generally very low. Moreover, UBS's credit was rated at the highest of levels by the rating agencies. Until the middle of December 2008, for example, Standard & Poor's assigned a rating of AA to UBS's liabilities. As a result, it was easy for UBS to obtain funding in the lending and capital markets at favorable terms.

The short-term funding obtained from the markets was distributed within the bank with no additional risk premium, regardless of the risks that the individual business units intended to assume. The bank and individual business units were therefore able to make risky investments while obtaining funding at very favorable terms. The difference between the borrowing rate and the returns received from the investments improved UBS's trading results. This business imploded when lending markets dried up during the financial market crisis, as it was no longer possible to obtain funding at favorable rates.

- *False sense of security despite warning signs:* Toward the end of 2006, that is, approximately one year prior to the outbreak of the financial market crisis, it became apparent that the growth in the US real estate market might be turning into a speculative bubble.

These concerns were not shared by UBS. Up to July 2007 UBS believed, falsely as it turned out, that its investments in predominantly high-quality investment products with high credit ratings (super senior, AAA and AA) were safe. With regard to its "origination and underwriting" activities, that is, the purchase, bundling and resale of structured financial products, UBS believed that the lower-rated investment products it held in its "warehouse" could be sold on the market at any time (cf. below page 21 f.). Moreover, UBS expected that any cooling of the US housing market would affect only investment products with the lowest ratings and

not the financial instruments it was holding, which had received top ratings by the rating agencies.

Because of these assumptions, which in retrospect turned out to be incorrect, UBS neglected to take measures which, with the benefit of hindsight, would have been adequate to limit its risk in the US housing market.

- *No overall assessment of risk positions:* The management of UBS's Investment Bank was aware of the individual positions held by business units that invested in US mortgage products, or bundled and resold these products. However, each business unit independently specified and monitored its own investment strategy, and no uniform assessment of the associated credit and default risks was performed at the divisional or group level. As a result, the Investment Bank was not aware of the extent of its default risk exposure until the end of July 2007.
- *Reliance on information from business units:* Up to the end of July 2007, the Group Executive Board of UBS and the senior management of the Investment Bank were confident, based on statements made by the responsible heads of the business units, that risk management and risk control were being performed properly with regard to products linked to the US mortgage market. It was only at the end of July 2007 that clarity was established in the Investment Bank as to the extent of its risk positions. The Chairman's Office of the Board of Directors and the Group Executive Board were informed of the situation on 6 August 2007. Prior to that time, the bank's Board and the Group Executive Board had assumed that the models used for the valuation of the risks of investment products linked to the US housing market were accurate and that the measures taken to limit risk were adequate.
- *Overreliance on statistical models:* As it turned out, UBS's specialists in the risk control area placed too much trust in statistical models (cf. above page 18). Their reliance on these models (stress tests and value-at-risk analysis) lulled corporate management into a false sense of security and shifted attention from the fundamental underlying risks in the US housing market. In retrospect, too much confidence was also placed in the rating agencies and the top ratings they assigned to certain investment products.
- *Remuneration:* The remuneration models used prior to the financial market crisis did not distinguish sufficiently between added value created by talented employees and income generated by exploiting market advantages, such as low funding costs. Performance-based remuneration was determined based on revenues, without adequately taking into account the sustainability of the income, or the risks associated with it, in connection with decisions regarding remuneration. In addition, the former model left virtually no possibility for demanding the restitution of remuneration once it had been allocated to employees.

C. How did the supervisory authorities deal with the crisis?

1. Investigation by the Swiss Federal Banking Commission

a) Subject of the investigation

In addition to that of UBS, the SFBC also performed its own independent investigation into the reasons behind UBS's write-downs in the course of the financial market crisis.

The SFBC based its investigation, in part, on the already mentioned 700-page report that UBS had submitted on 4 April 2008. In addition, the SFBC performed its own investigation and interviewed, in particular, the key decision-makers of UBS in meetings that lasted several hours. Such interviews were conducted with Marcel Ospel, Chairman of the Board of Directors of UBS until April 2008; Marco Suter, who was a member of the Chairman's Office of the Board of Directors until September 2007 and then group chief financial officer until September 2008; Peter Wuffli, group CEO until July 2007; Marcel Rohner, group CEO from July 2007 to February 2009; Huw Jenkins, CEO of the Investment Bank from June 2005 to September 2007; Walter Stürzinger, group chief risk officer from January 2001 to September 2007; Richard Metcalf, chief risk officer of the Investment Bank from June 2006 to June 2008; and Markus Ronner, head of Group Internal Audit (GIA) from January 2001 to June 2007.

The SFBC presented the results of its investigation in its report, "UBS AG and the Subprime Crisis", dated 24 September 2008. The report is 120 pages in length and was classified as confidential by the SFBC. The SFBC summarized the results of its investigations for the public in its report, "Subprime Crisis: SFBC Investigation Into the Causes of the Write-downs of UBS AG", dated 30 September 2008 (SFBC UBS Subprime Report).

b) Causes for UBS's losses

In the SFBC's view, the causes for UBS's losses during the financial market crisis were the following:

– *UBS governance decisions/strategy*: In the SFBC's view, certain governance decisions made at the Board of Directors and Group Executive Board levels, such as the creation of DRCM or the Investment Bank growth strategy (cf. **above page 21**), were defensible at the time they were made, even if in retrospect they took a wrong direction or were not properly implemented. However, the fact that UBS remained unaware, up to the beginning of August 2007, of the nature and scope of the risks it was exposed to in the subprime and related sectors, and that it was therefore unable to react quickly with suitable countermeasures, demonstrates that there were flaws in the organization.

The SFBC feels that the growth strategy followed by UBS's Investment Bank acted as a kind of catalyst in this regard. The pressure to catch up with its closest competitors in the fixed income sector created a climate that facilitated a number of undesirable developments. After the decision was

made to close DRCM, the management of the Investment Bank and the Group Executive Board were occupied with the task of reintegrating DRCM's positions and business organization. In the SFBC's opinion this was one of the reasons why the individuals concerned did not concentrate on what, in retrospect, were more important aspects of the bank's governance.

– *Lack of balance sheet limits / favorable refinancing*: The SFBC states that UBS, throughout its existence, has never understood the balance sheet as a tool for controlling risk appetite. Limits that placed restrictions on total balance sheet assets were not introduced until mid-2007, which, from today's point of view, was too late. The SFBC takes the view that the lack of attention paid to the hidden risks associated with growth in balance sheet assets and an overly uncritical reliance on the existing tools for identifying risks have led to the severe consequences that followed.

The possibility of obtaining favorable funding combined with a lack of control over the balance sheet then gave rise to a number of unfavorable developments. As a large international bank with top credit ratings, UBS was able to obtain credit and capital market funding at favorable terms. The funds obtained in this way were distributed to the individual business units without the addition of risk premiums. In the SFBC's opinion, this undifferentiated pricing model with respect to internal capital allocation led to a lack of sufficient incentive for using risk-return profiles in the analysis of business strategies. Efforts to introduce a differentiated pricing model for the business units were not actively pursued before March 2007, and did not lead to changes until after this date.

– *Risk management / risk control*: According to the SFBC, one of the main reasons for the massive write-downs was that the individuals who traded in, valued and monitored the positions in question failed, in retrospect, to accurately assess the risks inherent in subprime investment products and relied too heavily on the high ratings assigned by the rating agencies.

Until the summer of 2007 and according to standard international practice, subprime positions with high external ratings required little regulatory capital. Moreover, the risk management system only recorded net positions. Positions considered to have been sufficiently hedged based on model calculations were reported as minimal risks, even if the hedge was only partial (covering only for the first losses incurred on a position, for example). According to the SFBC, the individuals responsible for risk control at UBS were unable to completely determine the scope of the risk exposure that had been assumed. By the time this situation had changed and it was recognized that the previous appraisal of the situation did not reflect the true risks, the crisis had already broken out. In the end, it turned out that the various stress scenarios that the Group Executive Board had used as

their main tool for managing risk had been too optimistic. The stress calculated using historical statistics proved to be much less severe than the real stress that occurred due to market volatility. UBS – like other participants in the financial markets – failed to realize that it was exposed to a major macroeconomic risk due to the sheer magnitude of its total holdings in positions related to the US housing market or to US consumer behavior in general.

The SFBC concludes that the enormous write-downs that UBS was forced to take could not be attributed to any single factor. Rather, an entire series of what were, in retrospect, unfortunate strategic decisions, a failure to dig deeper and a lack of skepticism toward the bank's processes and systems had to be taken into account.

c) Assessment by the SFBC

In its overall evaluation, the SFBC states that it agrees with UBS's analysis with respect to the weaknesses that were identified. In particular, the SFBC states:

"Careful analysis of reasons by UBS: The SFBC agrees with the bank's analysis with respect to the weaknesses that were identified."

SFBC UBS Subprime Report, page 15

However, the SFBC also further concludes that UBS had been deficient in identifying, limiting and monitoring its subprime risks. This finding relates to UBS's governance, business and control processes in its entirety, although in differing degrees. Not all of the weaknesses listed were a sign of inadequate organization, poor management or deficient governance when taken on their own. What was important to the SFBC's conclusion that the organization was inadequate was the unsatisfactory outcome of their interaction.

In summary, the SFBC states that although UBS as an organization had infringed the obligation of proper management conduct as required under banking law, the currently responsible individuals (the question did not come up in connection with former directors and officers) were not liable under supervisory law.

"Breach of the proper management requirement by the bank: Not all of the weaknesses listed are a sign of inadequate organization or poor management when taken on their own. In addition, the fact that the introduction of balance sheet limits was discussed repeatedly, but also rejected repeatedly is not in conflict with supervisory law and can be justified in terms of business policy. However, the benefit of hindsight allows us to conclude that UBS failed to properly identify or adequately limit or monitor the risks associated with its super senior securities and other ABS securities in its warehouse and trading books. This is a serious failure and as a whole must be evaluated as a breach of the requirement of proper business management under banking law. The SFBC investigation did not, however, reveal anything that would lead to the conclusion that current directors or officers of the bank have breached the requirement to ensure proper business management."

SFBC UBS Subprime Report, page 15

The SFBC notes, in particular, that its investigation had revealed no information to suggest that UBS managers had willfully intended to cause damage to the bank, or had deliberately assumed incalculable risks solely for the sake of receiving higher bonuses. There was also no indication that the individuals responsible for risk control were aware of the risks that had been assumed but had deliberately turned a blind eye to them. On the contrary, everything suggests that the individuals responsible for building up the problem positions had full confidence in the presumed viability of their risk management system, so that they still believed that they were sufficiently hedged even when the markets had already begun moving sideways and downwards.

The SFBC also notes that UBS was not alone in incorrectly assessing the risks it had assumed, but that practically all participants throughout the entire market had made the same errors. The supervisory authorities themselves had also failed to recognize the impending danger in time.

2. Investigation by the SIX Swiss Exchange

As mentioned above, the public was first informed of problems associated with the impending crisis on 14 August 2007, and on 1 October 2007, UBS announced its third-quarter write-down, on the order of 4 billion francs (cf. above page 18). At that point in time, UBS was the first international bank to provide information on the nature and scope of its losses in the US real estate market.

Switzerland's stock exchange (SIX Swiss Exchange, SIX) opened a preliminary investigation into UBS in which it wished to examine whether UBS, as a listed company, had complied with its duties to disclose price-sensitive information ("ad hoc announcements"). UBS cooperated fully with the preliminary investigation.

In July 2009, SIX informed UBS that formal investigation proceedings would be initiated against UBS for a possible breach of the provisions relating to ad hoc announcements. This was publicly announced in a press release on 18 September 2009.

By letter dated 10 August 2010, SIX Exchange Regulation requested that UBS respond to a sanction request for breach of ad hoc publicity requirements. The proceedings are currently still pending.

3. Investigations by foreign supervisory authorities

Starting in the fall of 2007, the US capital market supervisory authority, the Securities and Exchange Commission (SEC), also conducted an investigation of UBS in parallel with the SFBC investigation. The investigation concerned questions relating to the information of market participants and of the valuation of positions in the US real estate market. Because UBS shares are also listed on the New York Exchange, UBS is also subject to SEC supervision.

UBS instructed the well-known law firm of Sullivan & Cromwell to respond to the reproaches made by the SEC. Sullivan & Cromwell presented its report to UBS, the SEC and the Swiss Stock Exchange on 3 March 2008. Until present, the proceedings have neither been officially closed nor did the SEC order any specific measures against UBS.

D. What measures has UBS taken to ensure that such losses do not recur?

1. UBS action plan

When UBS submitted its report on the causes of the financial market crisis to the SFBC in April 2008 (cf. above page 20), it also discussed the implementation of extensive organizational measures within the bank. The purpose of these measures was to ensure that the deficiencies identified in risk management and risk control would be remedied.

These measures were listed first in a 14-point project plan, and further in a comprehensive 38-page report entitled "UBS's Write-Downs Arising from the Market Dislocation: Lessons Learned and Remediation (Remediation Plan)", which was submitted to the SFBC on 6 June 2008.

UBS made the findings of the Remediation Plan available to its shareholders and to the wider public in the form of a ten-page summary published on the UBS website on 12 August 2008. The summary describes the measures that UBS introduced in the areas of "strategy", "corporate governance", "risk management", "risk control and finance", "funding and balance sheet management", and "compensation" (cf. below page 27 ff.).

In its own public report issued on 30 September 2008, the SFBC states that the measures introduced by UBS were adequate:

"The measures presented by the bank in its report to shareholders of 12 August 2008 are welcome and, in the view of the SFBC, appropriate."

SFBC UBS Subprime Report, page 15

The report, "UBS Plan for Risk Management & Control Renewal (Renewal Plan)", was issued internally within the group on 3 September 2008. The Renewal Plan restates the lessons that UBS drew from the financial market crisis and its causes (cf. above page 22 f.), and uses them to derive organizational and corporate governance objectives for the bank. The objectives and the measures to be taken thereon also fall into six categories: "strategy", "corporate governance", "risk management", "risk control and finance", "funding and balance sheet management", and "compensation".

Based on an SFBC order to this effect, UBS provided FINMA with regular reports on the status of implementation of the measures in the areas of risk management and risk control.

The objectives and measures in each area are summarized and discussed in the following pages. An overview is provided in the table below:

Root cause	Area	Lessons learned	Measures
Growth strategy	Strategy	<ul style="list-style-type: none"> – Business planning process – Strategic review processes – Investment governance 	<ul style="list-style-type: none"> – Strategy and planning processes changed to ensure increased rigor and better consideration of capital, funding and risk – Regular business reviews and portfolio risk reviews – Investment optimization processes strengthened in the IB
Governance			
Balance sheet limits	Governance	<ul style="list-style-type: none"> – Risk committees – Succession planning – Integrated approach to risk management and control – Technology investment 	<ul style="list-style-type: none"> – Recomposing the Board of Directors and the Group Executive Board – Differentiation of responsibilities between Board of Directors and Group Executive Board – Succession planning for top positions improved
Refinancing			
Signal interpretation	Risk management	<ul style="list-style-type: none"> – Risk management at the front – Capital allocation – Risk appetite and limits 	<ul style="list-style-type: none"> – Principles for risk standards and requirements and financial figures determined at broker level including monitoring processes – Risk appetite and risk limits determined depending on the risk capacity – Validation and monitoring of achievement of objectives for business plans
Overall assessment of risk positions	Risk control and finance	<ul style="list-style-type: none"> – Organization and instruments of risk control – Procedures and processes 	<ul style="list-style-type: none"> – Comprehensive identification of risks – Valuation rules and models reviewed and adapted – Development of integrated reporting for management purposes
Reporting	Funding and balance sheet	<ul style="list-style-type: none"> – Financing model and cash-flow management 	<ul style="list-style-type: none"> – Asset and liability committee established at group level – New financing-risk management framework incl. liquidity reserve for group; cost transparency by way of funding and liquidity costs – Limits for balance sheet positions with target amounts
Risk models			
Compensation	Compensation	<ul style="list-style-type: none"> – Compensation principles – Incentive structure 	<ul style="list-style-type: none"> – Compensation systems for members of the Board of Directors, Group Executive Board members and employees with special functions have been revised – Individual objectives and performance appraisal for employees improved
Subprime report	Lessons learned report		Remediation Plan

2. Strategy

a) Objectives

The internal investigation showed that certain growth strategies specified by the Board of Directors should have been better planned, in particular the growth strategy followed by the Investment Bank. The renewal plan included three objectives in the area of strategy:

- Business process planning should be strengthened and should place more weight on capital allocation, liquidity procurement and accounting for risks.
- Management processes should include regular reviews of business activities (business reviews) and UBS's portfolio risks (portfolio risk reviews).
- Investment decisions should be better organized to improve supervision of compliance with internal bank priorities, financing activities and the implementation of "change the bank" initiatives.

b) Measures

The following measures, among others, were taken in this connection:

- As an emergency measure, the CEO of the Investment Bank reviewed the portfolio of each business area in terms of its future need for resources (capital, financing, risk). These resource needs are now given particularly close attention in the entire strategy and planning process.
- The CEO together with the heads of the business units now ensures that comprehensive risk reviews are performed at regular intervals. These reviews are designed to take account of the macroeconomic environment, changes in market conditions, portfolio composition and risk concentration.
- In working out its strategy in 2009, the new leadership not only subjected the priorities and activities of all business units as well as the organizational structures to a thorough examination and realignment, but also deliberated in depth on the question of the UBS corporate culture. Its overriding objective thereby was to create a new UBS capable of sustainable high performance.

3. Governance

a) Objectives

In the area of governance the Renewal Plan demanded that the composition of the Board of Directors and the structure of its committees be examined and the processes at the Group Executive Board level be improved. In this connection, the Renewal Plan highlights four main points.

- The committee structures, formerly in place both at the group level and on the level of the Investment Bank level, must be revised.
- Succession planning for the most important functions within the bank should be professionalized.
- Risk management and risk control should be better integrated.
- The system architecture of the Investment Bank should be generally reviewed.

b) Measures

In relation to the framework of the new corporate governance, comprehensive staff changes have taken place and the tasks and responsibilities of the Board of Directors on the one hand and the group management on the other have been clearly defined.

- The most important measure is that, since the beginning of the financial market crisis, UBS has fundamentally recomposed its Board of Directors and Group Executive Board. A significant number of the new members of these boards were recruited from outside the company. The experience that they acquired in other financial service companies is now being used to the benefit of UBS. This led to a good mixture of internal and external expertise.
- At group level, there is now a clear separation of the responsibilities between the Board of Directors and the Group Executive Board. In July 2008, a Risk Committee was formed at the Board of Directors level, composed of independent directors. The Chairman's Office has been abolished.
- Within the Investment Bank, the risk committees have been given extended powers.
- Succession planning for the most important functions within the bank has been improved; suitable candidates for senior positions are now regularly identified and appraised.
- Various internal initiatives serve to shape risk management and risk control as an integral task of the bank. The new UBS has also streamlined the assignment of responsibilities. Prior to the financial market crisis, specialists, for example in the area of risk control, often had two superiors – the CEO of the business unit as line manager and a specialist in the area of risk control. However, the structures have now been simplified and harmonized. Each chief risk officer now has only one superior and the risk control of the group is independent of the business divisions.

4. Risk management

a) Objectives

During the internal investigation, UBS recognized various problem areas that concern the processes of front office risk management. The Renewal Plan identifies three areas which, as the crisis has shown, must be improved:

- Harmonization and improvement of the risk management at front office.
- Improvement of the capital allocation by introducing a risk-based assessment of the profitability of business activities of the bank.
- Group-wide risk appetite and risk limit regulations.

b) Measures

The following measures, among others, were introduced as part of the implementation of the Renewal Plan:

- The recording of positions, their valuation and the assessment of their corresponding risks and effects on the profit and loss account are performed on a group-wide basis in keeping with uniform principles.
- The CEO and the chief risk officer of the Investment Bank establish comprehensive principles for the risk standards and

requirements at individual business unit levels. In this connection it is required that each desk be in a position at all times to explain its balance sheet (including risk positions) and all features of its profit and loss account.

- The bank improved the procedure to perform continuous ex-post monitoring of complex products and transactions as well as the processes for the early identification of risk concentrations.
- Limits on the maximum holding period for positions and on portfolios and single transactions have been introduced.
- Business plans are now assessed on the basis of uniform criteria applicable both at the group level and the level of the individual business units and are subject to critical review at regular intervals. Whether the targets set are achievable is regularly reviewed by the CEO and individual members of the Group Executive Board.
- The reports systematically compare the income and expenses of the individual business units with projections, so that corporate management can swiftly recognize and correct possible undesirable developments. In order to assess the bank's overall performance, as well as that of its employees, key performance indicators – such as economic profit – are now systematically applied (**cf. on this page below**). These key performance indicators will have an increasing influence on the decisions regarding remuneration.

5. Risk control and financial aspects

a) Objectives

As regards risk control and finances, the company learned its lessons with respect to the organizational structure, the instruments used to ascertain the bank's risks, the relevant consent procedures for transactions, valuation issues, the quality of the management information available and the corresponding reporting. The Renewal Plan proposed numerous improvements in each of these areas.

b) Measures

The following measures, among others, were introduced:

- In the framework of risk control organization, the distinction between market risk and credit risk, as made prior to the financial market crisis, has been abolished. This allows the recognition and valuation of risks in an integrated manner.
- The valuation rules and models used internally by the bank have been and will be thoroughly reviewed and improved where necessary. This applies in particular to value-at-risk calculations, stress tests, and the monitoring of valuation and accounting models.
- The quality and frequency of reporting for the profit and loss statement of the bank are being increased.
- Expansion into new business sectors is now subject to more stringent controls.
- Senior management is actively involved in the examination and approval of large and high-risk transactions.
- The procedure for pricing positions in the trading book are being continuously revised to ensure that they are valued

and recorded in the bank's books in a timely and independent fashion.

- The bank is currently developing its integrated reporting solution that provides relevant management information. This solution contains, in addition to the financial data relevant for publication, further key information such as risk-adjusted profit contributions, the significant risks and the resources made use of by the business divisions.
- The harmonized and integrated reporting system now provides a monthly performance update report to all members of the Board of Directors and of the Group Executive Board. This report analyzes the bank's business performance and sets out in detail the relevant internal and external risks to which the bank is exposed.

The report not only discusses the financial situation and the market and credit risks of the bank but also the liquidity management and the active financing, operational, reputational and legal risks. Furthermore, monthly stress tests are performed for the entire group, including an analysis of the implications of any major events for the bank.

- At the Investment Bank level, a comprehensive framework of position limits has been introduced to limit market and issuer risks. Monitoring by the senior management has also been increased in that information on the Investment Bank situation is provided to the CEO at least once every two weeks.

6. Funding and treasury management

a) Objectives

As mentioned above, prior to the financial market crisis, the business units of UBS were able to refinance themselves at favorable conditions as a result of the overall circumstances prevailing at that time (**cf. above page 22 f.**). The financing model then in use did not, however, take sufficiently into account the risks emanating from the funds borrowed. Furthermore, there were no aggregate limits with respect to certain balance sheet positions (**cf. above page 22 f.**).

The Renewal Plan thus proposed that decisions regarding investments and financing be centralized at group level and at business division level. The internal liquidity management and funding regulations had to be redrafted and increased attention was to be paid to the risks in connection with group-internal fund allocation.

b) Measures

The following measures, among others, were taken:

- The Group Executive Board now also constitutes the Asset and Liability Committee (ALCO) at the group level. This committee is responsible for allocating balance sheet limits, risk-weighted assets and capital to the individual business units. ALCO also approves internal group financing.
- The company has introduced limits on total asset growth and on risk-weighted assets both at group level and at the level of the Investment Bank. Further, the bank has refined the reporting for purposes of overseeing balance sheet and liquidity use, and has introduced risk-adjusted calculation of financing costs.

7. Remuneration

a) Objectives

The UBS Shareholder Report discussed a few factors regarding the remuneration structure that could have contributed to the subprime losses. The Renewal Plan thus carried out an extensive review of the principles of remuneration with a view to placing more weight on the sustained development of the bank.

b) Measures

Implementing the Renewal Plan, UBS agreed with the SFBC in November 2008 that the assessment principles would be redefined and oriented specifically toward sustainability and long-term compensation. UBS announced the key features of the new remuneration model on 17 November 2008 and published it on its website. The remuneration model was subjected to a further critical review in September 2009 and was revised both with respect to the objectives as well as with respect to the structure of the remuneration.

The overriding objective is now to bring the interests of employees, in particular those in senior management positions at UBS, more in line with the objectives of the shareholders, and to take account of risk control when determining remuneration. This is done, first, by shifting the basis of variable compensation to an increased emphasis on the so-called economic profit. The bank's interpretation of economic profit is profit before tax less the pro rata cost of capital in the business division concerned. Considering the pro rata capital costs makes it possible, in particular, to take into account to a reasonable extent the risks in a business unit when measuring the performance criteria and determining the remuneration in that business unit. The performance of the managers, who have been identified by

the bank as risk takers, will be subject to particularly stringent controls. On an individual level, risks and their management will be incorporated into the agreement on objectives and performance appraisals and thus reasonable account will be taken of them when determining remuneration.

In addition, UBS pays remuneration increasingly in the form of shares and equity-related instruments. For example, for the financial year 2009, UBS decided that, above a certain threshold, at least 60 percent of performance-related remuneration would be share-oriented, in part with graduated payment, and at most 40 percent would be cash-based.

Finally, UBS has reformed its basic remuneration principles compared to the time prior to the financial market crisis in the sense that variable remuneration in some cases contains a malus component or even a forfeiture of the allocated remuneration. In particular, a malus is recorded if a loss results at the group or division level or an extremely large adjustment needs to be made to the consolidated balance sheet. A malus can also be recorded for some managers if gross violations of compliance regulations or violations of risk management guidelines are identified. In particularly severe cases, deferred remuneration is forfeited in its entirety.

Employees whose total compensation exceeds a certain threshold and who receive part of their performance-related remuneration in the form of shares, will not receive this part immediately but rather in installments over at least three years. In the case of the members of the Group Executive Board, the deferred part of the remuneration in shares can also be increased or decreased, depending on whether the agreed targets of the so-called economic profit (corporate added value) and the total shareholder return were reached by the end of the vesting period.

III. US cross-border wealth management business

A. How did the issues with the US authorities arise?

1. UBS's cross-border wealth management business

UBS serves clients all over the world. Some of UBS's clients are served by branches in the countries in which these clients reside. This business is referred to as "onshore business". Other clients have an account with a UBS branch outside of their country of residence; these clients are served on a cross-border basis by way of so-called "cross-border" or "offshore" business. As is the case for most other Swiss banks, the cross-border wealth management business is an important line of business for UBS. In addition to its network of branches in Switzerland, UBS has branches in all key European financial centers and in the US, Hong Kong, Singapore and in other countries. These branches have been serving clients both locally and on a cross-border basis for many years.

The business area that was the subject of the investigations conducted by the US authorities is the US cross-border wealth management business through which UBS serviced US-resident clients (US cross-border business). The US cross-border business was operated, on the one hand, by UBS branches in Switzerland and, on the other hand, by UBS branches abroad located outside the US. In Switzerland these clients were mainly served by a specialized department of the Americas International unit, with some 40 to 60 client advisors. The business in general had been declining since 2000 and with approximately 1 percent of total assets under management, the US cross-border business constituted only a very small part of UBS's entire wealth management business.

The US cross-border business must be distinguished from the much larger and separately-run wealth management business that a US subsidiary of UBS operates in the US. This on-shore business became more significant when UBS took over the US stock brokerage and asset management company Paine Webber in the year 2000. The matters discussed in this chapter bear no relation to these on-shore activities.

2. Legal framework

When providing services to clients resident in the US, not only Swiss law, but also US law, must be observed, in particular the provisions of the US securities laws and US tax law.

a) US tax law

In general, the US impose taxes on everyone in relation to certain income from US securities (dividends and interest). In the case of so-called "US persons" (US citizens or persons resident in the US; US taxpayers), such income is taxed on a net income basis. In the case of so-called "non-US persons" (foreign citizens not resident in the US, so-called "Non-Resident Aliens" or "NRAs") such income is generally subject to a withholding tax of 30 percent of the gross amount, subject to reduction under applicable Double Taxation Treaties (DTTs).

US tax law provides for the following to ensure that such income is correctly taxed:

- In the case of US taxpayers, the entity making payment of dividends, interest or sales proceeds (so-called "Paying Agent") must provide information reporting to the IRS about the payments stating the recipient's name and the so-called taxpayer identification number. If the Paying Agent is not in a position to do so, it must deduct withholding tax, the current rate of which is 28 percent, from the gross amount (so-called "Backup Withholding Tax") and remit such tax to the IRS.
- In the case of NRAs, the Paying Agent is required to deduct US withholding tax of 30 percent of the gross amount subject to withholding unless the NRA is resident in a country which has concluded a DTT with the US. In this case, depending on the provisions of the applicable DTT, a lower rate (often 15 percent or even less) of US withholding tax may apply.

In the 1990s, the IRS was concerned that the ability of the US to properly tax revenues with respect to US securities held in accounts at foreign banks suffered from the following weaknesses:

- First, the residence of an NRA was not used to determine whether a DTT applied, but rather the address of the foreign bank through which these NRAs held their US securities. This enabled clients of banks located in countries which had concluded a DTT with the US (for example Germany, the Netherlands, England) to benefit from a lower rate of US withholding tax even though the country in which these clients were resident (for example Saudi Arabia) had not concluded a DTT with the US. This practice of exploiting more favorable DTTs was referred to as "Treaty Shopping". This was, however, not possible in Switzerland since Switzerland was already collecting and providing to the IRS, on the basis of the old DTT with the US from the year 1952, in addition to the ordinary withholding rate of 15 percent, a further withholding tax of 15 percent (the so-called "Additional Withholding Tax USA") from all clients with respect to income from US securities.
- Second, US Taxpayers could hold US securities through accounts at foreign financial institutions without the income derived from such securities and their identity being reported to the IRS, provided they were prepared to accept a US withholding tax rate of 30 percent on dividend or interest income from such securities.

b) Qualified Intermediary Agreement

Toward the end of the 1990s, in order to address these weaknesses, the IRS completely revised the US withholding tax system which led to the establishment of the so-called "Qualified Intermediary System (QI System)".

The “Qualified Intermediary Agreement (QI Agreement)” was of central importance to the QI System. This is a standard agreement drafted by the IRS which foreign banks could conclude with the IRS. The QI System and the QI Agreement came into force on 1 January 2001. In total, in addition to UBS and almost all other Swiss banks, over 6,000 financial institutions worldwide decided to adopt the QI Status

If a foreign bank concluded a QI Agreement with the IRS, the bank (the “Qualified Intermediary”, or “QI”) was authorized to determine the applicable US withholding tax rate for its NRA account holders in accordance with the relevant DTT without reporting the identity of the account holders to the IRS or any US intermediary. If the client is a US taxpayer, the client is required to provide the QI with an IRS Form W-9, in which he informs the QI of his US taxpayer identification number, and the QI is required to provide such form to the appropriate Withholding Agent or to perform information reporting including the client’s identity to the IRS with respect to income from US securities earned by such client. If the US client refuses to execute a Form W-9 and the QI is prohibited by law from disclosing the identity of its account holders, the QI has to ensure that the client does not hold any US securities in its accounts with the QI.

The QI Agreement thus allows a foreign bank to grant NRAs who wish to invest in US securities the advantages of lower withholding tax rates, in accordance with the respective applicable DTTs, without having to disclose their identities to the IRS. Moreover, the QI Agreement allows foreign banks that are prohibited by law from disclosing the identity of their account holders to maintain securities accounts for US Taxpayers as long as they ensure that those US Taxpayers who do not consent to their identity being reported to the IRS do not hold any US securities in such accounts. In turn, the QI Agreement imposes far-reaching documentation, notification and withholding tax collection duties on the QI. Whether these provisions are being observed must be reviewed at regular intervals by independent auditors. From a Swiss perspective it is of importance that the QI System recognizes and preserves the Swiss banking secrecy.

In this connection, it is worth noting that the US is planning to amend the QI System in accordance with recently enacted provisions of the US Internal Revenue Code commonly referred to as the Foreign Account Tax Compliance Act (FATCA). These provisions essentially provide that foreign financial institutions whose clients intend to invest in US securities and who wish to benefit from applicable DTTs will have to obtain – by force of agreement with the IRS – consent from all US Taxpayers to disclose their identity to the IRS. This obligation applies independently of whether the US taxpayers invest in US or any non-US securities. Therefore, following the effective date of the FATCA provisions, US Taxpayers who are clients of foreign banks that have concluded such an agreement will no longer be able to hold US securities without consenting to the disclosure of their identity to the IRS, something that is still possible under the QI System. If the foreign financial institutions do not enter into an agreement with the IRS under FATCA provisions, the IRS will apply withholding tax at a rate of 30 percent on all income, including capital gains, that its US and non-US clients receive on US securities held at such financial institutions.

c) Financial market supervisory law

Anyone providing broker-dealer or investment advisory services in the US in return for remuneration is subject to various statutory requirements. Anyone involved in securities trading, providing investment advice or asset management must, for example, be registered and have a license. This also applies to any financial institution that conducts cross-border business in the US in which securities-related services are provided to US clients in the US irrespective of whether such services are provided to the client in a face-to-face discussion or by e-mail, telephone, fax or post (so-called “US Jurisdictional Means”). It is therefore not permitted, for example, without a license, to take an order in the US concerning the purchase or sale of shares or to provide advisory services with respect to securities. If such services are provided to a US client outside the US, for instance when he meets a client advisor in Switzerland, the US financial market supervisory law does not normally apply. On the other hand, asset management activity without a license is permitted if the US client enters into a discretionary asset management agreement in Switzerland and the Swiss bank subsequently carries out this agreement independently and exclusively in Switzerland.

At the beginning of this millennium, UBS, like practically all banks in Switzerland, was not registered with the SEC to provide securities-related services and was thus subject to the restrictions against providing unregistered securities-related services (SEC Restrictions). It was not until the year 2005 that a subsidiary of UBS, which was licensed with the SEC, commenced activities in Switzerland.

3. UBS’s US cross-border business between 2000 and 2007

Between 2000 and 2002, UBS was intensively occupied with, and invested substantial resources into, the implementation of the QI Agreement. This was an extremely complex and expensive process. Amongst other things it was necessary to obtain from all clients worldwide who held US securities in their UBS accounts, documentation that satisfied the requirements of the QI Agreement and, depending on the determination of the tax status of the client, to set up corresponding notification and withholding processes. This required extensive amendments to client documentation and adjustments of the internal processes and IT systems. The fact that numerous implementation details were unclear but could not be clarified by the IRS, or could be clarified only with delay, further complicated the situation. UBS also issued a number of internal guidelines intended to ensure compliance with the provisions of the QI Agreement.

A particular challenge existed in connection with legal entities that were not organized in the US (trusts, foundations and corporations), and which were defined under Swiss money laundering regulations as so-called “domiciliary companies”. Their treatment according to US tax law and the QI Agreement was and still is unclear. A central question concerned whether such domiciliary companies were to be treated as so-called “flow through” entities (the consequence being that such company’s income, pursuant to US tax law, would be treated as income of the beneficial owner of the company), or had the sta-

tus of so-called “non-flow through” companies. The latter had to file a so-called IRS Form W-8BEN and were therefore treated, pursuant to US tax law, as separate, non-US tax subjects. In this connection, UBS and other Swiss banks were particularly concerned with the question of how to deal with domiciliary companies held by NRAs that invested in US securities. If these were to be treated as “flow through” companies, according to the principles of US tax law and the QI Agreement, the identity of NRAs would have had to be reported – which actually would have been inconsistent with the QI System. When implementing the QI Agreement this fact led to a different treatment of domiciliary companies held by NRAs and domiciliary companies belonging to US clients.

On the basis of the SEC Restrictions and the QI Agreement, various models to serve clients residing in the US were available, including outsourcing the US client business to an external asset manager which would use UBS as depositary bank. During 2002, UBS finally decided on a model under which all existing business relationships with US clients would be converted into discretionary asset management agreements. In such cases, the client transfers the management of his assets entirely to the bank, and thereafter no longer instructs the bank as to individual investment transactions. At the same time, far-reaching restrictions were issued with respect to cross-border advice and accepting agreements to purchase or sell securities (so-called “Revised Business Model”).

Once the decision regarding the Revised Business Model had been made, the next step was to monitor the transfer of the approximately 3,000 US clients who had provided UBS with an IRS Form W-9 (and thereby consented to information reporting to the IRS) to a new subsidiary, which was registered with the SEC. These clients expected an all-encompassing service model which could not be properly guaranteed under the restrictions imposed by the Revised Business Model. Following the resolution by the Group Executive Board, early in 2004, to establish such a subsidiary, “UBS Swiss Financial Advisors AG (UBS SFA AG)” commenced operations on 1 January 2005.

In connection with the implementation of the Revised Business Model and the transfer of the so-called “W-9 clients” to UBS SFA AG, the services provided to US clients were centralized to a far greater degree than the services provided to the clients from other countries. The reason for this was the fact that the services to be provided to these clients were particularly complicated as a result of the SEC Restrictions and thus had to be provided by specially trained client advisors of the US Country Team.

In the year 2004, the instructions regarding US clients were placed on a new footing. In the same manner as for clients from other countries, the financial market supervisory law framework was set out in a “Country Paper USA” (Country Paper USA (2004)) – in the case of the US the above-mentioned SEC Restrictions – and rules of conduct were established. The Country Paper USA (2004) was the subject of training sessions and workshops attended by members of the US Country Team in the fall of 2004, and it was provided to all UBS employees on the intranet in the summer of 2005.

Further steps to reduce compliance risks were reviewed in the year 2006 within the framework of “Project Globus”. On

the basis of a presentation analyzing the US cross-border wealth management business, various measures were considered, including, among others, an even more extensive centralization of the US Country Team and travel restrictions. One of the possible measures mentioned was a complete withdrawal from the US cross-border business. In the end, seven of a total of 13 measures discussed were adopted, which, in the view of those responsible, were not expected to have any serious impact on the course of business. Other measures which might have further increased compliance with the SEC Restrictions were not taken.

On 17 March 2006, Bradley Birkenfeld, who had been employed since 2001 as a member of the US Country Team in Geneva, sent a letter to the then general counsel, Peter Kurer. In this letter Birkenfeld explained that, in the summer of 2005, he had discovered the Country Paper 2004, of which he had previously been unaware and which contained provisions diametrically opposed to the prevailing business conduct adopted by client advisors and required by line managers. Birkenfeld also stated that he had received no training with respect to the Country Paper USA (2004) and that his misgivings had so far gone unheard. The internal investigation ordered by Kurer, which was limited to the Geneva branch, reached the conclusion that, contrary to his assertion, Birkenfeld had indeed received such training. The investigation further confirmed that in some individual cases, clear – and in numerous other cases, potential – infringements of the Country Paper USA (2004) had actually taken place. Based on the results of the investigation report, Kurer ordered a series of new compliance measures, in particular, the revision of the Country Paper USA (2004), which was to be more clearly worded with specific “dos” and “don’ts”, and the introduction of effective compliance inspections. Although the first training sessions based on a draft of the new country paper took place in the fall of 2006, the final version only came into force in the summer of 2007 (Country Paper USA (2007)).

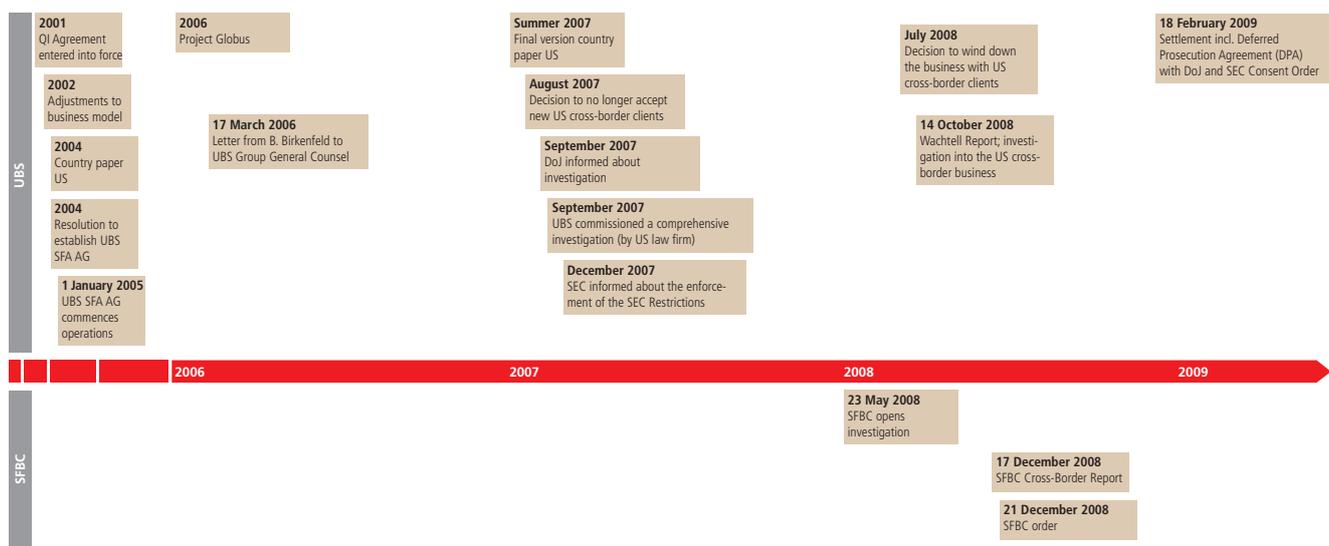
Parallel to the drafting of a revised country paper, UBS subjected the US cross-border business to a strategic review. As a result of the difficulties which had already emerged in connection with conducting the business in line with the SEC Restrictions, UBS resolved, in August 2007, to wind down the business with US clients: no new US cross-border securities accounts were to be opened and all US travel was to stop entirely.

4. Contact by the US authorities

In September 2007 the US Department of Justice (DoJ) informed UBS that it had been informed by Birkenfeld of shortcomings in the US cross-border business which had been the subject of an internal UBS investigation in the year 2006. Later that year, the DoJ also informed UBS that it had information according to which certain US taxpayers may have misused domiciliary companies incorporated outside the US in the context of the QI Agreement in order to continue holding US securities and that the SEC Restrictions had not been complied with. In December 2007, UBS was also contacted by the SEC, the authority responsible for the enforcement of the SEC Restrictions.

B. How did UBS handle the situation?

Chronology of reports and events – US cross-border business



1. Investigation by Wachtell, Lipton, Rosen & Katz

In response to the inquiries from the DoJ and the SEC, UBS immediately commissioned a comprehensive investigation with the objective of fully clarifying what had happened. UBS made it clear to all foreign and Swiss authorities from the outset that it intended to investigate all allegations swiftly and thoroughly and to provide them with a full report of the results, to the extent legally permitted.

Such investigations are commonplace in the US when allegations of potential corporate misconduct arise. They are generally carried out by law firms that are hired by the company concerned but are independent in carrying out their mandate. This conforms with the requirement of the US authorities which expect an objective, fact-oriented, and comprehensive report.

The investigation into the US cross-border business was carried out by the US law firm Wachtell, Lipton, Rosen & Katz (Wachtell). Wachtell is a leading New York law firm. An area of its activity for which it has received particular recognition is the conduct of investigations into possible corporate criminal and regulatory violations. Its expertise in this area derives, in particular, from the fact that several of its lawyers, including those responsible for the UBS investigation, are former federal prosecutors. Due to its experience and its commitment to conduct a careful and systematic investigation of the facts, the law firm enjoys a high degree of trust by the US authorities.

In order to guarantee that the investigation remained impartial, Wachtell reported, from summer 2008 onwards, directly and on a regular basis on matters relating to management liability to a Board of Directors' committee composed of the independent directors Sergio Marchionne, David Sidwell and Helmut Panke.

a) Scope and course of procedure

Based on extensive discussions with the US authorities in order to gain an understanding of their concerns and allegations, Wachtell focused its investigation on the years 2000 to 2007, concentrating, in particular, on the following two issues which were of central importance in terms of compliance with the QI Agreement and the SEC Restrictions:

- First: the circumstances under which, in the framework of the implementation of the QI Agreement, domiciliary companies controlled by US Taxpayers were set up for the purpose of holding US securities without notifying the IRS. In this connection the extent to which UBS client advisors were involved in these activities and whether the top management had knowledge hereof, tolerated such action or even promoted it, had to be investigated.
- Second: whether and to what extent the activities of client advisors violated the SEC Restrictions when serving clients. The subject of the investigation was, in particular, whether client advisors had provided securities-related services – including providing investment advice and taking securities-related instructions and transactional orders – to their US clients while in the US or by using telephone, facsimile or e-mail. The scope of the investigation also included the question whether the management of UBS was aware of such activities, had encouraged or at least tolerated them.

Wachtell investigated the relevant facts in the most comprehensive manner with the support of various specialists, including forensic auditors, IT specialists, etc. In addition to an analysis of all relevant transactions (including, for example, account openings and account movements) and the examination of relevant

account documentation, e-mails of more than 300 employees, agendas, protocols, instructions, memoranda and numerous other documents (in total approximately 1.5 million e-mails and other documents in electronic form were reviewed), several dozens of interviews of several hours' duration, were conducted with client advisors and other employees. The investigation team included some 100 members, both internal and external. It was one of the most comprehensive investigations ever conducted by a Swiss company in Switzerland.

The investigation was carried out exclusively on the premises of UBS in Switzerland and was conducted in accordance with the relevant provisions of Swiss data protection law and Swiss banking law.

The results of the investigation, the total costs of which amounted to more than 50 million Swiss francs, were compiled in a report dated 14 October 2008 (the "Wachtell Report"). The Wachtell Report, which is 170 pages in length, with numerous appendices, was submitted to the SFBC, the DoJ, the IRS and the SEC in mid-October 2008.

b) Conclusions drawn by UBS from the Wachtell Report

A review of the Wachtell Report led UBS to conclude that during the years 2000 to 2002, with the introduction of the QI System, it had undertaken substantial efforts to structure and document its account relationships with the account holders concerned to ensure that the requirements of the QI Agreement and US tax law had been fully complied with. For example, UBS had to contact roughly one million clients, in some cases more than once, in order to inform them of the requirements of the QI System and to obtain the required confirmations, instructions or forms from them. In the area of IT major adjustments had been made to enable the systems to identify US securities and to ensure that US clients who had not submitted an IRS Form W-9 could not hold any US securities. Moreover, US securities of US clients who did not respond to the request to submit an IRS Form W-9, were sold.

UBS made intensive efforts, in close cooperation with other Swiss banks and the Swiss Bankers Association, to satisfy the requirements of the QI Agreement through the framework of the instructions. These instructions were generally in line with the requirements of US tax law and the QI Agreement. In particular, they defined important differences with regard to the treatment of US clients on the one side and NRAs holding domiciliary companies on the other.

Within the bank, however, there had been instances of conduct contrary to instructions. It was established, for example, that certain UBS employees in the US cross-border business assisted US clients in setting up non-US domiciliary companies with the help of their external advisors, the aim of which was to enable the clients to continue holding US securities without submitting an IRS Form W-9.

Specifically a number of accounts were discovered which were opened for non-US domiciliary companies before the QI Agreement took effect. In these accounts, US securities in an amount of some 310 million francs were held. It was also established that some client advisors and their superiors had treated certain domiciliary companies as separate legal entities although they were aware that the necessary corporate require-

ments were not fully satisfied. In such cases the revenues deriving from US securities, pursuant to the QI Agreement, should have been treated as if obtained by the US beneficial owner of such entity (sham companies).

Also in subsequent years, other domiciliary companies had been set up for US clients in a number of cases in a similar manner without such practices being adequately reviewed or questioned.

As regards compliance with the SEC Restrictions, UBS ascertained that in the years 2004 to 2007 some 30 to 40 client advisors traveled regularly from Switzerland to the US for up to two-week visits and visited between 20 and 40 US clients on each occasion. While in the US the client advisors could access their clients' account information. A forensic analysis of the most important accounts of approximately 20 client advisors, along with numerous interviews with client advisors, confirmed that the SEC Restrictions were violated on a regular basis during business trips to the US and also during contacts from Switzerland.

The detailed investigations included various measures taken in the years 2001 to 2007 to bring the US cross-border business in line with the US tax laws and SEC Restrictions.

While UBS had made a substantial effort designed to achieve compliance with the SEC Restrictions, there had been deficiencies in the practical implementation of these measures. For example, in connection with the implementation of the Revised Business Model, UBS concluded that ultimately only some of the clients concerned were prepared to conclude a discretionary asset management agreement with UBS. Further, it took a long time for UBS SFA AG to become operative, the result of which was that so-called W-9 clients were serviced in repeated breach of the SEC Restrictions for a period of some three years.

Based on its analysis of the Wachtell Report, UBS concluded that insufficient attention had been paid to the compliance problems in the US cross-border business. The main problem had been the lack of effective oversight. There also appeared to have been deficiencies in terms of training and instructions and/or their implementation. For example, client advisors were aware that they were not permitted to accept any mandates from US clients during their visits to the US. However, it was generally assumed that other actions, such as the handing over of bank statements or investment documentation on US territory, would be tolerated by their superiors.

On a general level it was, however, established that client advisors assumed that a certain degree of non-compliance was unavoidable if the US cross-border wealth management business was to be maintained, and that this would be tolerated by their line managers.

As regards UBS's top management, UBS concluded that it was not reasonable to expect, given the fact that the US cross-border business represented a mere 1 percent of UBS's entire wealth management business, that they would follow the day-to-day operations of that business or be fully aware of the highly technical and complex aspects of the QI Agreement and of US tax and securities law as it applied to that business. In actual fact, the top management must, in principle, be able to rely on the responsible line managers and specialists from the tax and legal departments and from compliance to keep them informed

about important issues which require intervention by top management, and on them correctly implementing the instructions issued and the measures ordered.

2. Internal disciplinary investigation by UBS

At the beginning of 2009, UBS reviewed the conduct of employees from a disciplinary perspective on the basis of the results of the internal and external investigation and the applicable instruction framework including the responsibilities that such framework had determined. The decision of the required sanctions was taken by a group management committee which was composed of persons who had not been involved in the US cross-border business. The Board of Directors' committee approved these decisions. Both the US authorities and FINMA were informed of the measures taken. The authorities did not raise any objections.

The disciplinary measures affected approximately two dozen employees. A considerable number of employees who would also have been subject to disciplinary sanctions had already left UBS during the course of the preceding years. The disciplinary measures taken included dismissals, warnings and reprimands in combination with reductions in remuneration and promotion blocks. In addition to client advisors and their superiors, employees in other functions were affected.

3. Why did the problems in the US cross-border wealth management business occur?

UBS concurs with the assessment of the reasons leading to the problems in the US cross-border wealth management business as confirmed by the SFBC. Accordingly, in the Statement of Facts UBS has admitted responsibility for certain misconduct. Below, the main causes are again summarized, as seen from UBS's perspective:

– *Lack of a comprehensive and continuous risk analysis:* From 2000 onwards, UBS had increasingly identified the risks associated with the US cross-border business, both in connection with the implementation of the QI Agreement and with compliance with the SEC Restrictions. However, with a few exceptions, these two issues were addressed separately when assessing the risks and taking measures. Further, the risks resulting from the concurrent operation of both an onshore and an offshore business were not sufficiently considered. The consequences of different authorities jointly proceeding in order to enforce their respective regulations and increased risk profile of UBS due to its US operations were not adequately assessed in an overall context. Too much reliance was placed on the fact that the SEC historically had not strictly enforced the SEC Restrictions against foreign banks, and failed to implement adequate measures in a timely manner in response to the consequences resulting from the increasing focus the US authorities placed on the enforcement of their tax regulations and the growing domestic political pressure in the US.

– *Hesitant and incomplete implementation of measures:* Since UBS had identified, at least on an isolated basis, the risks attaching to the US cross-border wealth management business, senior management had decided to take various measures over the last years to ensure compliance with the relevant US regulations. However, there was a lack of rigor and speed when implementing these measures. This applies, for instance, to the adjustment of the business model in the year 2002, the preparation and the formation of UBS SFA AG and the implementation of the measures adopted following the investigation concerning Birkenfeld's whistle-blowing. Line managers in the US cross-border business focused on acquiring new business opportunities while too little attention was paid to the management of the risks associated therewith. Repeatedly, measures which had been decided upon were implemented only slowly and incompletely.

– *Shortcomings in the implementation of and in the continuous adherence to the QI Agreement:* UBS had implemented the QI Agreement largely in a correct manner and with enormous efforts. However, client advisors in the cross-border business were allowed too much discretion, and there was a lack of effective controls. Whether domiciliary companies were handled properly was often examined in a "form over substance" manner, without assessing whether in fact a sham company was involved. This allowed certain client advisors in a number of cases to assist clients in circumventing restrictions relating to the holding of US securities.

– *Insufficient compliance culture and lack of control:* UBS did not sufficiently pay attention to the complete and sustainable compliance with the complex regulations applicable to the cross-border wealth management business with clients residing in the US. There was a lack of effective control of the business, and shortcomings on the side of the employees involved were not vigorously rectified. There were also shortcomings in training and instructions as well in the structuring of the incentives. The internal regulations were imprecise and the expectations as regards compliance with these guidelines were not communicated with the required sense of urgency. This led client advisors to misconceive that a certain degree of non-compliance was tolerated by their line managers, which actually in part turned out to be the case. To a certain extent such business conduct did continue and remained undetected, as up until 2009 no independent controls were performed. Partly this was also the result of a governance structure which was not appropriately aligned to support a fully effective control framework. The compliance department responsible for the cross-border business was embedded in the organization of the CEO and the CFO of the Wealth Management & Business Banking division. Further, compliance with the country papers was not subject to the usual review cycles, since country papers were not considered as instructions in the formal sense.

UBS believes it has addressed these problems and their underlying causes by various measures (cf. below page 43 ff.).

C. How did the supervisory authorities react to the events?

1. Investigation by the Swiss Federal Banking Commission

a) Scope and course of procedure

The SFBC was informed by UBS in December 2007 about the investigations conducted by the DoJ and the SEC. On 23 May 2008 it opened its own investigation into these matters.

The following four issues were the subject of the SFBC investigation:

- *Actively assisting with tax fraud*: Did UBS or employees of UBS actively participate in the tax fraud committed by their clients?
- *Submitting false declarations*: Did UBS, within the scope of its obligations as a QI or otherwise, submit false declarations or reports to the US authorities, in particular to the IRS?
- *Violations of the QI Agreement*: Did UBS violate the QI Agreement and if so, how serious were these violations?
- *Method of dealing with the legal and reputational risks*: How did UBS and its employees deal with the legal risks resulting from the cross-border business in the US within the framework of the QI Agreement?

The 161-page “SFBC report on the implementation of the Qualified Intermediary Agreement and on UBS’s cross-border services in the USA” dated 17 December 2008 (SFBC Cross-Border Report) summarized the results of this investigation and served as the basis of the order of 21 December 2008 directed against UBS (SFBC order) which concluded the SFBC’s extensive investigation.

The SFBC commissioned an authorized investigator who confirmed that the internal investigation of UBS was appropriate. On the basis of extensive investigations of its own, including questioning Wachtell attorneys and the employees involved in the UBS investigation, the authorized investigator concluded that there were no indications that the former UBS management had influenced the internal investigation. Finally the authorized investigator was commissioned to write a report on the Swiss financial market’s traditional attitude toward selected aspects of the QI regime.

The SFBC was provided with the work products which had resulted from Wachtell’s independent investigation. For example, UBS provided the SFBC with the extensive documentation which had been compiled during the course of this investigation. This included minutes of meetings, legal opinions, audit reports by internal and external auditors, extensive collections of e-mails and personal documentation from individual employees questioned. The SFBC was granted access to all documents which were provided to the US authorities by way of administrative assistance. Furthermore, the SFBC had at its disposal the Wachtell Report and the comprehensive documentation on which this report was based. In addition, the SFBC requested UBS to submit further, more extensive documentation. Finally the SFBC interviewed over 20 UBS employees including Peter

Kurer, Group General Counsel (2001 to 2007), Marcel Rohner, CEO business group (Global) Wealth Management & Business Banking (2002 to 2007), Raoul Weil, head of business area Private Banking International and later Wealth Management International within the business group (Global) Wealth Management & Business Banking (2002 to 2007), Martin Liechti, head of business unit Americas International (2001 to 2007), Michel Guignard, head of business sector North America (2002 to 2007) and his predecessor Hansruedi Schumacher, head of business sector North America International (1998 to 2002).

b) Conclusions

(1) Implementation of the QI Agreement

The SFBC Cross-Border Report concluded that the efforts undertaken by UBS with respect to the entry into force of the QI System and in compliance with its duties as contractual partner of the IRS had been substantial and that UBS, despite the intense time pressure, had in general correctly implemented the QI Agreement. A few weaknesses had been detected where project organization and project management were concerned and, once these weaknesses had come to light in the year 2002, the project group was immediately reconstituted.

At the same time, the SFBC Cross-Border Report also pointed out that, in retrospect, there were other weaknesses in the implementation of the QI Agreement. In the SFBC’s opinion, the most significant weakness was that UBS assigned the responsibility for the execution of certain specific measures to the client advisors without monitoring their implementation activities. The lack of monitoring enabled individual client advisors (with the knowledge of middle management) to assist US clients in the misuse of non-US domiciliary companies which were created, controlled and managed by external advisors and asset managers for the purpose of continuing to invest in US securities (sham companies). In some cases, therefore, client advisors had assumed an active role in relation to the providing of (tax) advice to US clients which raised concerns about their potential participations in tax offenses. Furthermore, these activities were not compatible with the contractual obligations entered into by UBS vis-à-vis the IRS.

When implementing the QI Agreement, the line management responsible for the North America wealth management business failed to enforce a rigorous compliance culture, in particular with regard to wealthy US clients. However, the investigation did not reveal any indications that top management had knowledge of these breaches of the QI Agreement. In fact, UBS’s senior management took adequate measures each time it became aware of compliance problems in connection with implementation of the QI Agreement. According to the SFBC report, the fact that these deficiencies were not discovered at the highest levels for more than six years resulted from the responsibility for monitoring compliance with the obligations under

the QI Agreement not having been completely and clearly defined and, further, from a lack of sufficient control over the activities of those responsible for the US cross-border business.

In summary, the SFBC Cross-Border Report concluded that UBS as an institution violated the fit and proper conduct and organization as required under the Banking Act as it had taken risks that could be neither controlled nor monitored.

(2) Compliance with the SEC Restrictions

The SFBC Cross-Border Report concluded that UBS did not demonstrate a sufficient determination to comply fully with the SEC Restrictions. The SFBC noted that there were a few specific directions imposed by management relating to the US cross-border business which had direct implications for client advisors. These included, among others, the Revised Business Model, according to which discretionary asset management agreements should have been concluded with US clients, and directives that the rendering of advisory services and accepting orders relating to securities transactions in the US by telephone and e-mail was no longer permitted. Then, in 2004, the Country Paper USA (2004) was prepared which provided guidance relating to the SEC Restrictions and their application to the activities of client advisors. However, it was only after the revised Country Paper was issued in 2007 that monitoring of compliance with the instructions contained therein was introduced. According to statements made by the business area North America, this lack of monitoring was the result of the concern that such supervision would negatively affect the business.

Although UBS considered the traveling activities of its client advisors to be a practice that presented potential compliance risks, it did not oblige its advisors to confirm that they were observing the requirements set out in the Country Paper USA (2004). Measures to prevent client advisors from accepting orders for securities transactions during their visits to clients in the US or from meeting with potential clients in violation of the SEC Restrictions were either ineffective or not adequately enforced.

The reputational risks taken in this respect were not given sufficient attention. Apart from noting that there appeared to be a lack of interest by the SEC in enforcing these restrictions against foreign financial services providers, there was little evidence in the documents to show that deliberations had taken place on the consequences of failure to comply with the SEC Restrictions.

In the SFBC's opinion, UBS's decision to accept a violation of the SEC Restrictions with respect to delays in entering into discretionary asset management agreements with the clients when implementing the Revised Business Model was understandable. This was, however, no longer understandable in the period after 2007, as by that time it had long been common knowledge that these business practices were not fully in line with the applicable US provisions.

The SFBC held that UBS subsequently accepted that clients who had submitted a Form W-9 but did not conclude a discretionary asset management agreement were not subject to the restrictions of the Revised Business Model and could thus continue to be actively served. What was initially intended to be a temporary solution until UBS SFA AG had been established continued to be practiced for another three years. The problems

had been known since mid-2002, at the latest, by the line management responsible for the "Americas International" business. In the SFBC's view, it was incomprehensible that the bank did not take any additional measures to limit the resulting reputational risks.

The SFBC Cross-Border Report concludes that UBS took uncontrolled legal and reputational risks by tolerating violations of the SEC Restrictions and of internal instructions by client advisors and, as such, had violated its obligation to demonstrate fit and proper conduct and organization as required under the Banking Act.

(3) Organizational deficiencies

The SFBC Cross-Border Report also referred generally to unclear responsibilities regarding the issuance of internal regulations and the instruction and execution of compliance controls which ultimately was the reason that effective controls were not introduced. With respect to the – partially systematic – violations of the SEC Restrictions prior to the implementation of the US Country Paper (2007), the SFBC noted that management did not pay due attention to the specific legal and reputational risks.

According to the SFBC Cross-Border Report, the deficiencies that came to light during the course of the SFBC investigation had one common denominator: client advisors had been informed by various superiors to be flexible in individual cases and not to lose any clients. Within the North American business, a certain culture of ignoring and ignorance was therefore observed. Equally, as a general rule, there was no willingness to take appropriate measures to ensure compliance in day-to-day business operations.

Pursuant to the SFBC Cross-Border Report, the fact that client advisors were appraised mainly on the basis of the "Net New Money" criterion, as part of a new remuneration model, equally played a role. In the allocation of performance-based remuneration, this criterion was given excessive importance considering the practical impact of the Net New Money goal on the US cross-border business, inasmuch as it was only possible to achieve this objective by circumventing the restrictions that prohibited the client advisor from contacting his clients. While this problem was known to those responsible for the North America business, the top management of the Wealth Management and Business Banking division remained unaware of it due to insufficient supervisory procedures.

c) Responses to the questions investigated

In summary, the SFBC answers the questions raised in its report as follows:

- 1. Did UBS or employees of UBS actively participate in tax fraud committed by their clients?* The SFBC Cross-Border Report concludes that this cannot be excluded. It states that individual employees of UBS assisted US clients in the setting up of domiciliary companies for the purpose of enabling these US clients to hold US securities without submitting an IRS Form W-9, by which they would have been consenting to the declaration of their income to the IRS. This was not compatible with the terms of the QI Agreement. However, the SFBC Cross-Border Report also states that a final determination is possible only on the basis of a detailed analysis of the

conduct of the respective client advisors in conjunction with a review of their compliance with the applicable provisions of US tax law.

2. *Did UBS, within the scope of its obligations as a QI or otherwise, submit false declarations or reports to the American authorities?* The SFBC Cross-Border Report establishes that in certain cases in which US taxpayers chose structures involving domiciliary companies that should have been treated as “Flow-Through Structures” (and not as “Non-Flow Through Structures”), UBS, due to the particular circumstances, accepted an IRS Form W-8BEN submitted by the domiciliary companies instead of treating the US individual behind the structure as the beneficial owner for US tax purposes and reporting the individual to the IRS.
3. *Did UBS violate the QI Agreement and if so, how serious were these violations?* The SFBC Cross-Border Report establishes that violations of the QI Agreement did take place in connection with the transfers to newly established sham non-US domiciliary companies of US clients and with the restructuring of such companies. Furthermore, there were violations in cases in which, as a result of the direct contact between the US client, who was the beneficial owner, and the client advisor, the good faith of the bank with respect to the accuracy of the Form W-8BEN provided by the domiciliary company was destroyed.
4. *How did UBS and its employees deal with the legal risks resulting from the cross-border business in the US in connection with the QI Agreement?* The SFBC Cross-Border Report observes that the bank was increasingly aware of the legal and reputational risks associated with the US cross-border business. While ever more restrictive measures to minimize these risks were taken, it is clear, in retrospect, that they were taken too late and their implementation was not sufficiently consistent. At least for a certain time it was known at higher management levels that there were instances of non-compliance with the SEC Restrictions, which were seen as a temporary irregularity in need of remedy. Ultimately, however, this state of non-compliance lasted for a long time.

Furthermore, the management responsible for the US cross-border business accepted violations in connection with the implementation of the QI Agreement but took no action to report these legal and reputational risks to the supervising bank management.

d) Measures taken by the SFBC

The SFBC decided not to take measures against members of top management (so-called “fit and proper guarantors”). The SFBC order held that the serious deficiencies must be attributed to conduct by individual employees below the functional levels of top management. The highest corporate bodies were not aware of this conduct. In particular, the SFBC investigation did not reveal any indication of circumstances which would justify the issuing of a formal reprimand against responsible directors or officers individually or which would justify the taking of further supervisory measures. The fit and proper status of these persons was not questioned.

As regards UBS as an institution, the SFBC order states that the seriousness of the deficiencies discovered in connection with risk management and risk control justified the issuance of a formal declaration to this effect.

The SFBC order prohibited UBS from continuing to provide services to US taxpayers who did not submit an IRS Form W-9, and ordered that these client relationships be terminated as quickly as possible.

Further, UBS was placed under an obligation to adequately determine and record the legal and reputational risks when providing cross-border financial services from Switzerland. The measures implemented were to be reviewed by an independent third party by means of an audit conducted on behalf of the SFBC at a later point in time.

2. Investigations by the US authorities

The DoJ and the SEC have raised a number of allegations concerning the conduct of the US cross-border wealth management business and have carried out investigations into UBS from the point of view of US law. The US authorities used as the basis of their allegations documents which they had obtained from UBS, via the Swiss authorities, by way of administrative assistance, their own investigations, including interviews with Bradley Birkenfeld, Martin Liechti and other employees of UBS, and the Wachtell Report. Based on the results of their investigations, the DoJ and the SEC have come to the conclusion that, in UBS's US cross-border wealth management business, a series of mistakes were made. In the settlement with the DoJ, UBS expressly accepted responsibility for these mistakes in a “Statement of Facts”. In summary, the “Statement of Facts” contains the following:

From 2001 through 2007, UBS Private Banking employees traveled to the US to meet US persons resident there, and communicated with such persons with the aid of "US Jurisdictional Means" with respect to their (undeclared) accounts. They did so irrespective of the fact that certain US clients had chosen not to provide UBS with a form W-9 with respect to their UBS accounts and thereby concealed such accounts from the IRS.

In the same period, UBS employees contributed toward the US losing out on income tax by actively assisting or otherwise facilitating US taxpayers to conceal assets. In particular, the UBS employees arranged in individual cases for accounts to be opened by an offshore company, allowing such US taxpayers to evade reporting requirements and to trade and remain invested in US securities.

In connection with the establishment of such offshore companies, UBS employees accepted, in particular, forms W-8BEN provided by the directors of the offshore companies which represented under the penalty of perjury that such companies were the beneficial owners, for US federal income taxes, of the assets in the UBS accounts. In certain cases, the forms W-8BN were false or misleading in that the US taxpayer who owned the offshore company actually directed and controlled the management and disposition of the assets in the company accounts and/or functioned as the beneficial owner of such assets in disregard of the formalities of the purported corporate ownership.

Despite the fact that UBS was aware of the violations both of duties under the QI Agreement and of US regulations, these activities continued because of the profitability of the US cross-border business. It was for this reason that the decision to exit this business was only taken in August 2007. The implementation of such decision was further delayed.

An additional factor abetting violations of US regulations was UBS business unit "Wealth Management International" changing its compensation approach to take account of a number of factors, including new net money, which provided incentives to expand the size of the US cross-border business.

The employees working in Zurich, Geneva and Lugano who were responsible for the US cross-border business had contact with and serviced their US clients primarily during business trips to the US. They traveled to the US an average of two or three times per year, in trips that generally varied in duration from one to three weeks, and generally tried to meet with up to five US clients per day. On these business trips, they used encrypted laptop computers. While in Switzerland, they would communicate via telephone, fax, mail and/or e-mail with their US clients.

In the period between 2000 and 2007 UBS's US cross-border business provided financial services to approximately 11,000 to 14,000 US clients who had chosen not to provide a form W-9 or who were the underlying beneficial owners of offshore companies that maintained accounts with UBS. The US cross-border business of UBS generated approximately 120 to 140 million dollars in annual revenue for UBS and was a relatively very small part of UBS Global Wealth Management.

As certain US clients indicated that they wanted to continue to maintain their US securities holdings and not provide UBS with a form W-9 on behalf of the IRS, UBS issued written guidelines advising employees in the US cross-border business not to actively assist US taxpayers who may seek to establish domiciliary companies, and that any such companies should respect corporate formalities and not be operated as a sham. UBS internal documents also noted that active assistance by UBS employees to help US clients set up domiciliary companies to evade provisions of the QI Agreement might be viewed as actively helping such clients to engage in tax evasion. Notwithstanding those guidelines, certain managers in the US cross-border business thereafter authorized UBS employees to refer the US clients who did not wish to comply with the new requirements of the QI Agreement to certain outside lawyers and consultants, and did so with the understanding that these outside advisors would help such US clients form offshore companies for the purpose of tax evasion. UBS, through such referrals, indirectly assisted such US clients in creating and maintaining sham domiciliary companies. This enabled such clients to conceal their investments in US securities and thereby evade UBS's obligation to provide tax information reporting and to backup withhold with respect to certain payments made on such accounts.

In the period from 2000 through 2007, UBS adopted a series of compliance initiatives that were intended to improve compliance by the US cross-border business with the QI Agreement. In particular, UBS adopted written policies regarding the proper handling of accounts for domiciliary companies beneficially owned by US persons. It also took measures to prevent the provision of financial services in the US or with the assistance of "US Jurisdictional Means". However, UBS did not develop and implement an effective system of supervisory and compliance controls to prevent and detect violations of its policies. UBS failed to monitor and control the activities of certain of its employees, and as a result, some of these employees came to believe that a certain degree of non-compliance with UBS policies was acceptable in connection with operating the US cross-border business. Moreover, owing to the lack of corresponding monitoring measures, UBS was not able to determine the cases in which tax information reporting and backup withholding for payments would have been required.

The internal investigation had only a limited scope and did not follow up on available evidence. As a result, only isolated instances of non-compliance were detected, which could have been avoided if a comprehensive investigation (rather than one with a limited scope) had been conducted.

Source: Statement of Facts

The allegations by the SEC involving UBS are set out in the "Complaint" lodged by the SEC. The statement of facts in the SEC action against UBS is worded similarly and in part identically to the "Statement of Facts" in the DOJ action, which UBS acknowledged as part of the settlement of the DOJ investigation.

On 18 February 2009, the proceedings by the DOJ and SEC against UBS were concluded by means of a comprehensive settlement. This settlement included the conclusion of the already mentioned "Deferred Prosecution Agreement (DPA)" with the DOJ and the consent of UBS to a so-called Final Judgment by the competent court in the SEC procedure (SEC Consent Order).

In the framework of these settlements, UBS has essentially undertaken the following:

- to pay a total amount of 780 million US dollars;
- to complete its exit from the US cross-border business;
- to introduce an effective control program with respect to compliance with the obligations under the QI Agreement;
- to increase the independence of the legal and compliance functions, in particular with respect to promotion and compensation issues.

UBS also undertook, in compliance with an order addressed to UBS by FINMA in light of the threat of a criminal indictment in the US, to surrender information regarding account relationships of certain US clients.

An important component of the DPA was the DOJ's agreement to defer prosecution of any claim against UBS for a period of at least 18 months subject to certain conditions. If UBS properly fulfills all obligations under the DPA, the DOJ will ultimately dismiss with prejudice all possible claims.

Not covered by the settlements were the civil proceedings – the so-called "John Doe Summons" which had been initiated by the IRS, by which the IRS sought to obtain account documentation of all US taxpayers with account relationships with UBS in Switzerland. In August 2009, these proceedings were resolved by way of international agreements between the Swiss and US governments, and a related mutual administrative assistance agreement between the US, Switzerland and UBS AG.

D. What steps has UBS taken to ensure that the problems do not recur?

Beginning in the spring of 2008, UBS implemented comprehensive and far-reaching measures to ensure that the problems arising from the cross-border wealth management business would not recur in the future. It did this on four levels:

First, UBS completed its exit from the US cross-border business and introduced processes and monitoring systems in order to ensure that UBS consistently complies with US law with respect to all transactions with clients with links to the US. A US law firm continuously monitored the progress of the implementation of these measures, with the assistance of the auditing company KPMG, for the period of one year. The law firm recently confirmed in a comprehensive report to the SEC and the DoJ that implementation had been successfully completed.

Second, in the framework of an extensive project, UBS identified the risks arising out of the entire cross-border business and introduced numerous far-reaching measures to adequately monitor these risks. Some elements of this program are a direct response to the experience from the various investigations mentioned in this report. Others respond to more recent developments in the regulatory and political environment which affect the entire financial market. The entire cross-border business is currently in a fundamental transformation process. UBS has regularly informed FINMA about the implementation of these measures and FINMA will instruct an independent auditing company in the fourth quarter of 2010 to review the appropriateness and effectiveness of these measures.

Third, UBS has increased the independence of the legal and compliance functions and, fourth, it has introduced an effective monitoring system with respect to the obligations under the QI Agreement which was also reviewed by an independent auditing company, and the successful implementation of which has been confirmed to the DoJ.

1. Exit from the US cross-border business / US Settlement Execution Program

To ensure comprehensive and timely compliance with the obligations that it assumed under the DPA and the SEC Consent Order, UBS set up a dedicated project, the US Settlement Execution Program (Settlement Execution Program). The Settlement Execution Program has comprised, at times, more than 100 employees and reported to an Oversight Committee (OC) which was headed by the Group General Counsel and the CEO Wealth Management, both of whom are members of the Group Executive Board. The OC in turn reports to the Risk Committee of the Board of Directors.

The main tasks of the Settlement Execution Program include the execution of the exit from the US cross-border business and the development and roll-out of a policy and control framework in both Switzerland and other UBS locations worldwide to ensure continued compliance with applicable US laws and regula-

tions. Further, the Settlement Execution Program coordinates and exercises oversight with respect to compliance reviews at the Investment Bank and Global Asset Management.

a) Exit from the US cross-border business

To complete the exit from the US cross-border business, UBS first identified those account relationships that fell within the scope of the DPA and the SEC Consent Order. UBS has engaged in an intensive dialogue over the last twelve months with both the DoJ and the SEC to ensure full agreement with respect to the scope of the exit requirement under the DPA and the SEC Consent Order as well as under US laws. This dialogue led to certain amendments of the DPA and of the SEC Consent Order. On this basis, UBS was able to determine precisely which account relationships it was obliged to terminate and which businesses it was to re-structure in order to become fully compliant with US laws and regulations and guidance received from the SEC.

Second, UBS engaged in a thorough review of tens of thousands of account relationships to ensure that it had identified all those relationships that, according to its legal analysis and agreement with the US authorities, matched the relevant criteria. Where the quality of account data available was not such that a clear determination could be made, UBS engaged in remediation efforts to obtain the information needed to establish with certainty whether specific account relationships had, in fact, to be exited.

By 31 July 2010, the exit program had been largely completed. By that date, UBS was able to terminate approximately 90 percent of all accounts, covering approximately 95 percent of all assets that are subject to the exit. The remainder of the accounts consist mainly of accounts with products that cannot be readily liquidated, such as private equity investments, and, more importantly, accounts for which UBS has not been able to solicit an instruction to terminate the relationship as required under Swiss law. These accounts have been transferred to a special unit and are subject to tight controls.

UBS has also changed the service model relating to certain account relationships or products that are not subject to the exit requirement, in order to ensure full compliance with the SEC Restrictions based on new instructions from the SEC. For instance, based on such guidance, UBS is no longer accepting instructions relating to transactions in US securities from individuals residing in the US that hold a power of attorney over accounts of non-US persons.

b) Introduction and implementation of US Person Policy and related Compliance Control Framework

In addition to the execution of the exit from the US cross-border business, UBS has issued new instructions and implemented a control framework designed to ensure that UBS does not, in any of its locations, open new accounts for US clients in entities

that are not registered with the SEC. The key elements of this framework include the US Person Policy, mandatory training, client advisor certifications, account documentation requirements, compliance reviews and controls.

The US Person Policy is the core document that sets forth the fundamental rules, including a definition of which customers and services are affected by the DPA and/or the SEC Consent Order and to what extent the SEC Restrictions affect all other account relationships maintained by UBS globally. It further provides that UBS employees are, in principle, prohibited from traveling to the US for the conduct of business, that no communications regarding securities business may be sent to or received from the US, and that all UBS employees with client-facing or immediate supervisory or risk control responsibilities must be regularly trained, tested and certified with respect to the US Person Policy.

A broad range of detailed instructions, procedures and controls have been developed to implement the provisions of the US Person Policy. The key elements are as follows:

- As of November 2010, clients opening an account with UBS will be required to sign a declaration affirming whether they or any beneficial owners of the account are a US national, green card holder or US resident. Account holders must also undertake to inform UBS without delay if their or a beneficial owner's status should change. This measure will ensure that UBS will not open any account without knowing the status of the respective client under US laws.
- To date, over 17,000 employees have completed detailed mandatory training with respect to the implementation of the US Person Policy and procedures relating to the US Settlement Execution Program. Upon completion of the training and test, each such employee must certify that he or she (i) has read and understood the US Person Policy; (ii) will comply with that policy; (iii) acknowledges a continuing responsibility to review all client accounts to ensure that they are correctly coded with respect to US Person status; and (iv) understands that violations of the policy could result in serious disciplinary measures. The training and certification must be repeated by all such UBS employees at two-year intervals.
- Client advisors must also complete due diligence checklists for their clients, both when opening an account and when reviewing existing accounts. The client advisors must make a determination as to whether (i) the client is a US person, (ii) all relevant documentation has been received, and (iii) the client has been properly coded in the bank's systems.
- All direct line managers of client advisors must certify at least yearly that they have verified that all US persons in their area of responsibility have been properly documented and coded. Further they must confirm that all accounts subject to the exit have been transferred to a special unit responsible for terminating such account relationships.

UBS has also established a number of functions that have responsibility for oversight, investigation, review and support in relation to the implementation of the US Person Policy.

- A specialized legal team regularly reviews the US Person Policy framework and provides expert advice with respect to

all matters relating to compliance with relevant US laws and regulations.

- Compliance performs independent periodic reviews of accounts and required documentation and monitors compliance with US business travel and communications restrictions and training, testing and certification requirements. Compliance also regularly reviews files and client forms to identify accounts which may be in violation of the US Person Policy and to institute procedures to transfer or close such accounts.
- The US Competence Center, together with the project office, has a centralized reservoir of data, information and personnel with particular expertise, which maintains bank-wide statistical data on accounts with US Person status and provides assistance with the termination of accounts prohibited by the US Person Policy. The unit provides day-to-day advice on US Person issues and operates a web-based global portal, containing relevant policies and procedures, forms, contact information for relevant personnel, and other pertinent information.

2. Comprehensive measures to address and control risks associated with the Wealth Management & Swiss Bank cross-border business globally / Cross-Border Business Review Program

In addition to the measures taken in the US context, UBS embarked on a comprehensive review of all of its international businesses and took a series of additional measures to ensure that it adequately addresses and controls all related legal and reputational risk in all of its cross-border businesses. These reviews and measures involve not only UBS Wealth Management & Swiss Bank, but also other divisions, including Wealth Management US and the Investment Bank. However, given the growing fiscal and economic policy-motivated pressure on cross-border businesses operating out of jurisdictions with increased financial privacy protection, notably Switzerland, and the complexities of the legal and regulatory framework in which the wealth management businesses operate, this report focuses on measures taken in the Wealth Management & Swiss Bank division and its Cross-Border Review Program.

The program aims to review and, where necessary, revise, in consideration of all legal requirements, all instructions and controls applicable to the cross-border wealth management business, to adequately train the employees concerned and to adjust the products & services framework. It envisages a comprehensive treatment of all relevant legal and reputational risks. The program deals not only with business activities abroad, but also with cross-border services provided with "remote means" (i.e. by telephone, mail, fax, e-mail). Further, it (i) addresses compliance with product-specific investment restrictions, licensing requirements and offering rules; (ii) considers corporate tax, payroll tax, and client withholding and information reporting obligations under "permanent establishment" concepts; and (iii) explicitly addresses secondary liability for tax offenses (aiding and abetting, money laundering).

The program is centrally managed and operates along a number of workstreams, notably (1) Policies, (2) Control Framework, (3) Education & Training, (4) Products & Services, (5) Global Financial Intermediaries, (6) Wealth Planning Services, and (7) IT Tools and Processes. The program is under the control of the so-called "Cross-border Committee", in which all relevant units of UBS Wealth Management & Swiss Bank are represented.

a) Policies

Failures that occurred in the US cross-border wealth management business demonstrated the importance of a holistic governance, and they underline that the "rules of engagement" need to be clear and realistic. In response to these findings, UBS developed a comprehensive governance and policy framework. The basis thereof is a comprehensive framework policy (Global Cross-border Policy) which is, to the extent necessary, complemented with specific instructions (Supplementary Instructions). In the cross-border business, this policy framework is further supplemented by a number of additional regulations and directives, notably in the area of wealth planning services.

The Global Cross-border Policy describes the basic elements of the overall framework:

- It establishes a Cross-border Committee as the decision-making body for all material cross-border business issues and assigns clear responsibilities for the implementation of the cross-border framework, including regular controls.
- It establishes the requirements for a comprehensive control framework, including independent controls conducted by the responsible persons within the Compliance function.
- It requires that all employees dealing with clients on a cross-border basis be certified in accordance with a mandatory training curriculum, and it provides that employees are not permitted to embark on client-related business travel abroad unless specifically authorized to do so, with such authorization being granted only if the employee is trained and certified.
- It establishes general principles regarding tax and regulatory compliance and sets forth a list of expressly prohibited activities. These principles highlight that while it is generally not UBS's role, nor is UBS in a position, to verify whether clients are in compliance with the relevant tax obligations, employees must not encourage or assist clients in any scheme designed to breach their legal obligations including their tax obligations. These principles are supplemented by a number of activities which likewise are explicitly prohibited.

The Supplementary Instructions cover a number of countries, client segments (e.g. corporate clients), booking centers, and representative and advisory offices. They take the format of detailed "activity and product grids", addressing with specificity real life situations along the "life-cycle" of a client relationship with clear "dos" and "don'ts", covering three different scenarios: (i) the client comes to see the client advisor in the booking center, (ii) the client and the client advisor communicate by telephone, mail, fax or e-mail; and (iii) the client advisor travels to the client's country of domicile.

By the end of 2010, UBS will have completed Supplementary Instructions for 60 countries, covering 90 percent of UBS's client assets. In addition, specific instructions will be prepared for all relevant representative offices and a number of client segments.

b) Controls

One of the most important lessons learned in connection with the US cross-border wealth management business was the importance of effective compliance control processes. As a consequence, UBS has developed and implemented a comprehensive Cross-border Control Framework to support the enforcement of the Cross-border Policy. This consists of primary controls performed by the front office, IPS and other front facing functions together with independent controls undertaken by Legal & Compliance.

Controls have been designed and implemented in, among others, the following areas and issues: (i) travel (approval and pre- and post-trip briefing), (ii) training and certification of employees, (iii) remote communication, (iv) compliance with country-specific restrictions in terms of products and services offered, (v) dealings with external asset managers (FIMs), and (vi) activities of foreign representative offices. The results of these controls are regularly reported to senior management.

A key topic in this area is the control of cross-border travel activities. For this purpose, UBS has developed a so-called "Travel Approval & Control Tool (TRACT)" which not only supports the approval process but equally secures compliance with training requirements and facilitates independent controls by Compliance.

UBS will continue to develop the control framework to meet changing cross-border demands and to ensure that the key risks of its cross-border business are actively and effectively monitored. UBS will take disciplinary measures to sanction any failures to comply with these requirements.

c) Education and training

As the rules applicable to the cross-border business are complex, UBS puts special emphasis on providing its employees with a training framework to ensure that they know and understand these rules. The education framework that has been developed includes the following main elements:

- A mandatory general web-based training is designed to assist employees to understand and familiarize themselves with the Cross-border Policy. To date, this training has been successfully completed by over 17,500 employees globally.
- Mandatory country-specific web-based training programs are based on the Supplementary Instructions and cover, in detail, the specific rules and regulations applicable to a specific country. Country-specific web-based training programs are now available for 28 countries, and they have been completed by more than 6,000 client-facing employees.
- Classroom desk head training programs ensure that desk heads fully understand their responsibility as supervisors of client advisors and enable desk heads to coach their teams and ensure proper implementation of the policy framework. To date, these mandatory training programs have been completed by over 650 desk heads.

d) Products and services

The Products & Services workstream is a response to the ever-increasing body of regulations in the cross-border business. It deals with product-specific investment restrictions, licensing requirements, offering and reporting rules applicable in the cross-border wealth management business and which, in UBS's view, will be of growing significance. On the basis of a detailed analysis of all applicable rules and regulations, the need for adjustments to product offerings is identified, and the required adjustments are implemented in order to ensure compliant product offerings in each country on an ongoing basis.

Given the complexity of the subject, efforts in developing a comprehensive locally compliant product shelf have been focused on a number of key markets. The product shelf analysis for remaining important countries will be concluded in the course of 2011. UBS has decided to support the implementation of these country-specific product rules by developing an appropriate IT tool for use by client advisors.

e) FIM business

The business with external asset managers and financial consultants (so-called "Financial Intermediaries", or "FIMs") is likewise the subject of the Cross-border Business Review Program. In this business, particular risks arise from the fact that this relationship consists of three parties (UBS, the FIM and the end-customer), and more in particular from the fact that contacts with the end-customer (whose assets are deposited with UBS) take place almost exclusively between the FIM and the end-customer. To address these risks, UBS has introduced the Global FIM Control Framework, the main pillars of which are as follows:

- a global Policy on Financial Intermediaries which defines minimum standards for the business. Importantly, UBS does not maintain relationships with FIMs that are non-operating companies or that are not properly licensed as required by local laws and regulations;
- booking center specific rules improve the due diligence process concerning the FIMs (background checks, examination of their licenses and internal rules regarding travel activities, etc.) before business relationships are entered into with the respective FIM.

In addition, UBS has started to roll out revised and enhanced contractual agreements (Framework Agreement Intermediaries) to further clarify the FIMs' responsibility as an independent manager with regard to clients. UBS will also organize so-called "awareness days" on cross-border topics for FIMs in order to assist them in understanding the complexities and challenges of engaging in cross-border business activities.

f) Wealth planning services

Unrelated to the US cross-border wealth management issue, UBS is reviewing its own offering in the area of wealth planning services. Wealth planning structures have been identified by fiscal authorities as "red flags" for activities which are considered as open to misuse in certain circumstances. UBS has taken a number of measures to address these concerns.

UBS is of the firm view that there are many legitimate reasons why high net worth clients might wish to take advantage of wealth planning services and these remain a very important element of UBS's wealth management services offering.

The new rules and regulations provide that UBS will no longer provide trusts, foundations and life insurance policies to its clients where client advisors have knowledge, or reasons to suspect, that the product is to be used as a means to enable the beneficial owner to commit a tax offense or otherwise breach relevant regulations.

Further, clients have to confirm, when seeking UBS's wealth planning services, that UBS does not provide advice with respect to foreign tax laws and that they have obtained independent legal, tax and other professional advice as appropriate and necessary.

In the view of UBS, the above measures appropriately protect the legitimacy of the services offered and the position of clients requesting them.

g) Further measures

Given the complexities of the cross-border servicing requirements and the resultant challenges that arise for its employees, UBS has decided that, wherever possible, international clients should be served by units specializing in the client's country of residence. This country-specific segmentation will not only improve the quality of the services offered to the clients, but equally improves the ability of the client advisors to apply the rules, as they will be able to focus on one country, or a small number of countries, thereby mitigating risks and strengthening control capabilities. This country-specific segmentation is currently being handled by a dedicated project, covering all major markets, including foreign clients with accounts maintained in UBS's Swiss branch offices.

3. Changes to the governance of Legal & Compliance

In recognition of the importance of the full independence of the Legal & Compliance function, UBS has centralized the reporting lines within the Legal & Compliance function under the leadership of the Group General Counsel. This also applies to the members of the compliance function who are responsible for the independent controls within the wealth management business. These newly centralized reporting lines to the Group General Counsel are designed to ensure that legal advice and the execution of controls are immune to attempts to exercise undue influence on the part of those responsible for the businesses under review.

Crisis management and reorganization processes were accompanied by a reinforcement of the legal and compliance functions on all levels. This provides more flexibility to the Group General Counsel in supporting the cultural changes currently underway within UBS.

Further, UBS has revised the framework for remuneration and promotion matters relating to Legal & Compliance personnel, taking into account the independence requirements applying to a control function. Under the revised framework, the bonus pool is allocated in aggregate to the group general counsel who then, in turn, allocates to his direct reports who pro-

pose individual salaries and bonuses. The Group General Counsel retains the final authority with respect to compensation and promotion of Legal & Compliance personnel, and neither divisional management nor anyone else outside of Legal & Compliance has the authority to override the Group General Counsel's final authority on these matters.

UBS has also reorganized its compliance function. A Global Head of Compliance was appointed with a mandate to define the overall compliance strategy for all business divisions and regional units, ensure that systemic and significant issues are identified and addressed and that adequate compliance-related processes, policies and procedures are in place and provide consistency across all businesses. Under this reorganization, a number of functional teams were established to enhance group-wide recognition and control of specific risks. A central compliance function was established to deliver global compliance processes.

4. Improvement of governance and of the control program relating to the implementation of the QI Agreement

In order to meet various commitments UBS has made under the DPA, UBS has also strengthened its governance and the control program in relation to its obligations under the QI Agreement:

- First, UBS introduced several new functions and staffed them with specialized personnel, such as the position of a Group Head US Withholding and QI Compliance and of a QI Tax Coordinator.
- Second, UBS has enhanced its written policies and procedures to reinforce various aspects of QI compliance. In particular, with respect to client documentation requirements, UBS policies and procedures go beyond the requirements of the QI Agreement.
- Third, UBS has strengthened various controls to prevent, detect, and correct material failures under the QI Agreement.
- Fourth, UBS has improved and intensified training of relevant personnel on various QI requirements.

The implementation of the steps described above was confirmed by the independent audit firm KPMG in a 49-page report to the DoJ, dated 16 June 2010.

IV. Liability issues

Based on its investigations, the SFBC as supervisory authority has reached the conclusion that UBS, as an institution, did not observe the principle of proper management during the financial market crisis on the one hand, and in connection with the cross-border wealth management business on the other. However, the SFBC did not conduct proceedings against individual persons; in the course of its proceedings directed against UBS, the SFBC did note that, based on the available information, there was no basis for proceeding against individual members of the former UBS corporate bodies with a view to potential infringements of the principle of proper management.

However, the question remains as to whether legally relevant charges can be made, pursuant to Swiss law, against individual former directors and officers of the bank. The question has been raised, for example, as to why the prosecution authorities

have chosen not to prosecute any former directors and senior officers. Equally, there has been much public interest focused on the question of why the Board of Directors of UBS decided not to file a civil suit against its former directors and senior officers. The CCs of the Federal Assembly even raised the question of whether the Confederation should provide financial assistance for directors' and officers' liability claims.

The decision on the potential financing of civil proceedings by the Confederation is ultimately in the hands of the authorities. This report, therefore, does not address this issue further. Rather, this report will set out and explain the reasons why UBS has decided not to file liability claims against former directors and officers. It will further discuss why UBS has decided not to take steps to initiate criminal proceedings in connection with the US cross-border business.

A. Claims under civil law against former directors and officers

1. Preconditions for a director's liability claim under civil law

A failure of risk control in the US mortgage business or insufficient compliance within the group organization with respect to the US cross-border wealth management business do not automatically lead, under civil law, to liability on the part of members of the management or Board of Directors. Rather, the statutory conditions for a claim must be fulfilled in order to successfully hold a former director or officer accountable.

Four conditions must be satisfied cumulatively for a corporate body to be liable: breach of the duty of care, an actual loss, a so-called causal connection between the breach of duty and loss and a fault for which a director or officer is personally responsible.

– *Breach of the duty of care*: The board of directors, as a body, and its members are required by statute (article 717 subsection 1 of the Swiss Code of Obligations) to carry out their tasks with due care and to loyally safeguard the interests of the company. In doing so, the board of directors must focus on the interests of the company with the aim of furthering the long-term financial benefit of all stakeholders (small and major shareholders, employees, etc.).

To the extent that the board of directors does not deal directly with business matters, but delegates them to a management board, the board of directors is not directly responsible for the fulfillment of these delegated duties, but only for the careful selection, instruction and supervision of the persons to whom these duties have been delegated. The same principle applies to the members of the group executive board. The courts tend to consider the duty of care from an objective point of view and compare it with the conduct one would expect of a person acting with the care of a prudent businessman in a comparable situation.

The duty of care performed by members of a corporate body is thus evaluated on the basis of the knowledge he or she had at the time of the conduct in question. The circumstances at the time the decision was made are thus taken into account. If, in retrospect, it appears that a different decision would have been preferable or more adequate than the one actually taken, pertinent case law does not suggest that liability automatically results. Poor corporate decisions – those which subsequently result in losses – are not automatically incorrect decisions which lead to legal liability. The courts recognize that a board of directors is under an obligation to take corporate decisions in the interest of the company and that, as a consequence, certain risks may have to be taken.

– *Loss*: If a breach of the duty of care by individual members of the board of directors or the group executive board has been established, the injured party must prove in a second step that specific damage, that is, a financial loss, resulted directly from this breach of the duty of care.

If the company suffers a financial loss as a result of conduct in breach of the duty of care, the company itself suffers direct damage corresponding to this loss. The loss leads to a drop in the share price, resulting in the shareholder suffering damage only indirectly, as he or she still holds the same number of shares in the company. The Swiss courts do not consider a drop in the inherent share value to constitute direct damage to the shareholder. A shareholder who has not directly suffered a loss in his or her own assets can thus file a claim only for payment to the company.

In the case of UBS, it must also be noted that the events which caused damage to UBS's assets occurred to a large extent as a result of the financial market crisis, and, therefore, cannot be attributed to acts or omissions by the directors and officers of UBS. A claim for damages, therefore, can seek recovery only of that part of the loss that was caused directly by a breach of the duty of care by the directors and officers.

– *Causal connection*: In considering a directors' and officers' liability claim, the courts must decide, among other factors, whether there is a so-called adequate causal connection between the breach of the duty of care and the loss incurred. Only if the breach of the duty of care has led directly to a specific loss can the responsible director or officer be held liable for such loss.

The causal connection between a loss and a breach of the duty of care can be interrupted if an event has occurred that completely overshadows all prior contributory factors. Under such circumstances, it is no longer possible to attribute a specific loss to the breach of the duty of care. In each individual case, one has to specifically determine which part of the damage actually suffered resulted from which contributing factor.

– *Fault*: If it can be established that a breach of the duty of care was the direct cause of a quantifiable loss, it is an additional requirement that a member of the board of directors or of the group executive board can be personally held responsible for such breach. Under Swiss corporate law, any responsible directors or senior officers are only liable for their own personal violations of the duty of care, that is, for faults they themselves have committed, and for resulting losses.

No individual can be held personally liable for the faults of others. The conditions for liability must be proven for each individual director and officer against whom a claim is filed – in particular an individual breach of the duty of care and individual responsibility (fault). The fact that the SFBC has established that UBS as a bank did not comply with the principle of proper business management does not automatically give rise to personal responsibility of individual persons who managed the bank at the time in question.

In addition to these four conditions for liability, a series of further considerations must also be taken into account prior to asserting liability claims against directors and officers.

- *Who can be the subject of a claim?* Directors' and officers' liability under corporate law requires that the persons being held responsible are directors or officers. Members of the board or of the group executive board who have a full voting right at board meetings do hold the status of directors or officers.

Managers below the group executive board may qualify as officers if they are assigned executive management duties and can thus decisively influence the decision-making process of the company. This is especially the case if a person carries out transactions and makes decisions that go beyond routine day-to-day business and which are of corporate significance and have an impact on the status of the company. Employees at lower levels who are bound by instructions are not, as a rule, regarded as officers – even if they make decisions in the preparing or implementing of decisions by the group executive board.

- *Who can file a claim?* Every shareholder is entitled to file a claim. However, he or she may only claim direct compensation if he or she has suffered a loss of his or her own assets. If his or her position is that acts and/or omissions of a director or officer caused a loss for the company, the claim is for payment to the company.

However, statute also provides for the possibility of the company itself filing a claim. Such a claim can be initiated by the board or by a decision of the shareholders at a general meeting. Claims filed by the board against former directors and officers of a company are extremely rare in Switzerland. If the shareholders resolve to file a claim, such a resolution must be placed on the agenda of a general meeting and be approved by a majority of the shareholders present or represented.

As a general rule, a shareholder who files a claim against directors or officers bears the risk of the resulting costs. If his or her claim fails, he or she must bear his or her own costs and the costs of the court and additionally compensate the opposing party for its legal fees. It is a tradition in Switzerland and in the rest of continental Europe for the losing party to bear the costs. In the most recent discussions in connection with the introduction of the new Swiss Federal Code of Civil Procedure, this principle has not been questioned. However, the law provides that the court can allocate the costs between the plaintiff and the company if the circumstances justified the filing of the claims (article 756 subsection 2 of the Swiss Code of Obligations).

If the company files the claim and fails, it bears the procedural costs. This applies irrespective of whether the decision to file a claim is taken by the board or by the shareholders at a general meeting.

- *Statute of limitations and forfeiture.* The general limitation period for claims based on corporate directors' and officers' liability is five years from the time of knowledge of the loss and of the person liable. In addition, there is a general statutory limitation period of ten years which begins to run when the breach is committed.

If the shareholders have discharged the board for a financial year at a general meeting, no further claims can be made by the company against its directors and officers for this fi-

ancial year. Shareholders who have not consented to the discharge must file a claim within six months; otherwise they forfeit their right to a claim. However, this rule does not apply with respect to facts which were not known at the time of discharge. It further does not apply in UBS's case to claims which refer to acts or omissions by the former directors and officers in the financial year 2007, as the shareholders have not discharged the Board for this financial year at the general meeting held in April 2010.

Liability is not presumed, but must be proved. In court proceedings the burden of proof is on the plaintiff: he or she must explain in detail and prove that each of the conditions for liability has been satisfied.

2. Investigations commissioned by UBS

To begin, the Board of Directors of UBS examined whether the above conditions of liability under corporate law were satisfied in the case of the directors and officers concerned. This question had to be examined both in connection with the events relating to the subprime losses as well as to the US cross-border wealth management business.

Already in October 2008, the Board of Directors of UBS appointed a committee of independent members to assess the risks and chances of directors' and officers' liability claims. The committee consisted of the then Vice Chairman of the Board of Directors, Sergio Marchionne, and Bruno Gehrig, who had just been elected as a member of the Board. In preparation for the decision by the Board, the committee mandated two renowned Swiss law firms – Homburger AG (Homburger) and Bär & Karrer AG (Bär & Karrer) – to prepare legal expert reports on the question of liability in relation to the subprime losses. In addition, Bär & Karrer investigated the criminal law implications of the US cross-border wealth management business and the question whether there was a reasonably good likelihood of success for liability claims in this area. All legal expert reports were also made available to the SFBC. As set out below, in November 2009 the Board of Directors decided to refrain from bringing actions against the former senior managers and directors. This decision was publicly announced on 15 December 2009.

Following the publication of the CCs' report and in the course of the preparation of this report, the Board of Directors decided to commission an independent expert review of its decision to refrain from bringing actions against the former senior managers and directors. It mandated this task to Prof. Peter Forstmoser, an authority in the field of corporate law and an acknowledged expert in questions concerning directors' liability under corporate law. Prof. Forstmoser had access to all internal and external investigation reports referred to in this transparency report as well to the expert reports of Homburger and Bär & Karrer. Based on these documents he assessed two questions: First, whether the decision of the Board of Directors to refrain from initiating legal action against the former directors and officers was made on the basis of sufficient information. Second, whether this decision was justifiable, or even required, from a corporate law standpoint.

3. Liability claims in connection with the financial market crisis

a) Expert report by Homburger

In October 2008, UBS instructed Homburger to render an opinion, on the basis of the existing investigation reports and without further fact-finding efforts, regarding the possibility of filing directors' and officers' liability claims against former directors and officers of UBS. Homburger assessed in particular whether, on the basis of the investigations already undertaken, there were specific indications of individual misconduct by individual directors or officers of UBS or whether the Board needed to investigate the matter further.

This report was handed over to UBS on 27 October 2008.

Homburger pointed out that the Board of Directors of UBS was obliged to be guided by the interests of the company when considering whether to file liability claims against former directors or against former executives. In this context, the Board of Directors needed to consider any possible further consequences of an action, e.g. costs and benefits thereof, negative impact on the reputation of the company, or the fact that an action would divert management's attention from day-to-day business.

b) Expert report by Bär & Karrer

After reviewing the expert report prepared by Homburger, the Board's independent committee acknowledged, as an interim conclusion, that in accordance with the expert report submitted by Homburger, further investigations were possible, but not compulsory. However, as a precautionary measure, the independent committee of the Board decided to commission a second thorough review of the facts. In October 2008, therefore, it mandated Bär & Karrer to carry out an in-depth investigation into the question of liability on the part of former directors and officers. Bär & Karrer was asked to independently verify the determinations and facts established thus far, and to carry out the internal interviews and document reviews that were necessary for that purpose.

Bär & Karrer subsequently spent approximately 2,000 working hours scrutinizing all of the investigations. The firm assessed whether the Board of Directors and the Group Executive Board ought to have realized the risks associated with its US mortgage business prior to August 2007 and should therefore have taken steps to limit or even downsize the bank's exposure.

Based on the expert report of Bär & Karrer, the Board of Directors of UBS had essentially four options in terms of how to proceed: to acknowledge the expert report and to take no further legal steps, to seek a settlement with the responsible persons, to stop further payments of bonuses or compensation to the persons responsible or to file a claim.

c) Assessment by the Board of Directors: Prospects of success of liability claims for the recovery of losses incurred in the subprime sector

After reviewing both legal expert reports, the Board of Directors of UBS, during summer and fall of 2009 and again when preparing this report, discussed the question of bringing actions against former directors and officers in connection with the subprime losses.

Neither the FINMA investigation nor the preliminary investigations by the public prosecutors produced findings that provided sufficient comfort that a claim would be successful. Even upon reviewing the expert reports commissioned by UBS, the Board of Directors had no sufficient certainty concerning the prospects for such actions.

The Board also noted – without any intent to seek excuses – that in addition to UBS, many other banks had been engaged in the mortgage business in the US, so that the risk estimates could not be considered as totally inaccurate, at least when viewed from the perspective of the time they were made.

Background

In this connection it is interesting to note that even in the USA where plaintiffs appear to find more favorable conditions than in other countries similar claims for damages have so far not been successful. Shareholders of Citigroup Inc., for example, filed suit against former directors and officers with the courts in the state of Delaware. Citigroup suffered losses in the amount of 124 billion dollars in connection with US mortgages and, following the collapse of Lehman Brothers, the US Federal Reserve was compelled to make further equity capital available to the bank and to provide guarantees for its high-risk investments. In a judgment dated 24 February 2009, the related shareholder claims were rejected.

The Board saw particular difficulties in successfully proving that the former corporate bodies individually and specifically violated duties of care and thereby caused specific losses. The chances of success were therefore considered by the Board of Directors to be low.

4. Liability claims in connection with the US cross-border wealth management business

a) Expert report by Bär & Karrer

Bär & Karrer was mandated to investigate whether there were reasonable prospects of success in bringing a liability action relating to the US cross-border business. These examinations were carried out on the basis of the results of the investigation by the SFBC and of the Wachtell Report. The aim of the assessment performed by Bär & Karrer was to review the Board's evaluation of the results of the SFBC report and its appraisal of the risks and consequences of any directors' and officers' liability claims from the point of view of experienced litigation lawyers and, if appropriate, to validate those conclusions.

The first question to be assessed was which of the persons who were active in the US cross-border wealth management business was to be qualified as an officer under corporate law, and thus as a proper defendant in liability proceedings. Since only the members of the UBS Board of Directors and of the Group Executive Board can be considered directors and officers for the purposes of article 754 of the Swiss Code of Obligations, neither the personnel and management of the North America division nor the client advisors and their superiors, up to the head of the business unit Americas International, can be qualified as officers. It was thus necessary to examine whether, based on the results of the investigations conducted so far,

there were sufficient indications that directors' and officers' liability claims could be successfully brought against individual members of these two boards who were responsible for the US cross-border business.

In summary, Bär & Karrer examined to what extent breaches of duty had occurred at the level of the Board of Directors and Group Executive Board. At issue, however, was not the active, intentional participation in unlawful acts on the part of subordinates, but omissions: deficiencies in the organization and in the implementation of measures, for which the Board of Directors and Group Executive Body were ultimately responsible.

b) Assessment by the Board of Directors: Prospects of success of liability claims for the recovery of losses incurred in the cross-border sector

Based on an assessment of the results of the comprehensive investigations and expert reviews, the UBS Board of Directors came to the conclusion that bringing liability actions would not serve the interests of UBS, but would, in fact, have detrimental effects. Their conclusions were as follows:

– As far as *breaches of the terms of the QI Agreement* are concerned, the fact is that written internal instructions of UBS to client advisors were available. These instructions among other things clearly stated that sham companies could not be accepted as beneficial owners under US tax law.

This leads to the question of whether the internal monitoring system for verifying compliance with these provisions by client advisors was adequate. The respective responsibility lay, however, with the direct superiors at a lower level in the line of responsibility, and not with members of senior management.

– As regards the *issue concerning securities trading regulations* senior management had recognized that there was a need for action to be taken. Specific measures were also resolved to remedy the irregularities that had come to light. However, implementation of these measures was in some respects too hesitant or did not take place with the necessary degree of consistency and there were no monitoring processes in place which would have made it possible to identify errors in the implementation of these measures.

The Board had to take into account that directors' and officers' liability claims would only have prospects of success if a specific person could be accused of specific breaches of duty which led to losses that can be quantified. Here, it had to be taken into account that, due to the specific circumstances, UBS would not be able to deliver the required elements of proof required for a successful claim. The central element of the reproach made to the directors and senior officers was that they had not taken steps to ensure that the measures they had decided upon for establishing a situation in compliance with the law were enforced with the speed and determination that was required. The accusation was not, in other words, that the members of top management themselves were responsible for the creation of the unlawful situation, but rather that they had failed to recognize this situation and to remedy it swiftly enough. Whether the delay in the implementation of the measures actually led to an additional loss that exceeded a loss that would

have resulted if the US cross-border business had been immediately abandoned is questionable.

The Board also acknowledged that with respect to the US cross-border business the experts had come to the conclusion that enforcing directors' and officers' liability claims against former individual members of the Board of Directors or of the Group Executive Board in court would entail significant litigation risks.

5. Further considerations by the Board of Directors

In addition to the arguments for or against the prospects of success in claims against former directors and officers of UBS – and this with regard both to the financial market crisis and the cross-border wealth management business – an entire series of further issues needed to be considered before a well-informed, comprehensive decision in the best interests of the company could be made. The question to be answered, in reality, was not simply whether litigation was likely to end successfully but also whether such litigation would make sense.

Other important arguments, unrelated to the likelihood of success, also led the Board to decide against filing claims against former directors and officers:

– *Actual result of a claim*: The Board took note of the fact that litigation, given the enormous litigation costs to be anticipated, as well as the resulting reputational damage, even if successful, would not serve UBS's interests. The amount of damages that could theoretically be recovered in such litigation would in any event be limited to the personal fortune of the respective defendants or to the amount of any available insurance coverage.

Several former directors and officers had waived the payment of substantial salaries and bonuses owed to them, or even voluntarily reimbursed them. For instance, Marcel Ospel, Peter Wuffli, Stephan Haeringer and Marco Suter have waived compensation totaling more than 70 million Swiss francs previously granted to them. Marcel Rohner as CEO of UBS waived his bonus in 2007 and 2008. The Board viewed this gesture as an indication that the former directors and officers of the bank had acknowledged their accountability, even if they were not to be held liable under the law.

– *Potential subsequent implications of litigation*: The filing of liability claims would have considerable negative consequences for UBS that would be beyond its control.

The relatively low financial benefit of a possibly successful claim must be set against the costs in the form of an increase in future insurance premiums. The potential defendants enjoy the usual market insurance covering civil liability claims, that is, they would not themselves bear the costs of court proceedings. Since UBS is required to offer such usual insurance cover to its current and future directors and officers, expensive court proceedings, if successful, would unavoidably lead to an increase in the amount of future insurance premiums.

Furthermore, it would have to be expected that in Switzerland and especially the US, free riders of all kinds would join in an action. US procedural laws do not provide that the losing party in a lawsuit has to indemnify the successful par-

ty for costs. Therefore, suit may be filed, even where there is small likelihood of success, without any major negative financial consequences for the plaintiff.

In addition, US procedural law allows for very extensive evidence-gathering measures (in particular, so-called discovery proceedings), which may compel a defendant bank to deliver to the courts and to the plaintiff all relevant documents, regardless of the substantial internal and external costs it may thereby incur. For this reason, many companies against whom suit is filed in the US prefer to settle out of court, even with plaintiffs whose case may be shaky, rather than assume the risks and expense of long and drawn out litigation.

Finally an action could result in a situation in which former directors and senior managers assign blame to and bring suit against each other, or they could extend the action to third parties. This would certainly not serve the interests of UBS or of its shareholders. Further, such a situation would result in incalculable reputational risks for UBS and have a negative impact for UBS in the proceedings in the US, which, in light of the long-standing business with US and other foreign clients, would be adverse for the entire Swiss banking sector.

- *Pending litigation in the US:* It must be kept in mind that class action lawsuits against UBS and former directors and officers are already pending in the US. In the opinion of the Board, the allegations made in these lawsuits are baseless, both with respect to the facts and the law, and are simply an attempt by lawyers specializing in this field to file exaggerated claims, with the hope of obtaining as high a settlement as possible.

By litigating against its former directors and officers in Switzerland, UBS would negatively impact its position in these class action proceedings in the US, in particular because, under US rules, the US plaintiffs could claim that this is an admission that they had in fact acted improperly. The Board of Directors has sought advice from its US counsel who have concluded that such a presumed acknowledgment of guilt would make it difficult to defend UBS's inter-

ests in these proceedings, and would potentially lead to an increase in the financial compensation that UBS would be obliged to offer in case of a settlement, even if the claims were without prospects of success.

It is important to note that UBS would have to bear these consequences at the same time that it commences litigation in Switzerland. The outcome of the Swiss liability lawsuit is of no relevance in this context: the mere commencement of litigation would result in the consequences outlined above, even if the claims brought in Switzerland were, in the end, to be rejected after years of litigation.

- *Position of the shareholders:* If the company were to initiate a lawsuit then, ultimately, the owners of UBS, that means its shareholders, would have to bear the costs associated with these proceedings in Switzerland and with potential proceedings in the US. Such a lawsuit, therefore, would have direct negative consequences for each individual shareholder without a realistic prospect of financial gain. The fact that the largest shareholders of UBS have never requested that UBS file liability claims against its former directors and officers supports the Board's assessment.
- *Looking to the future:* The Board appreciates that, from a Swiss perspective, considerations relating to pending or potential proceedings in the US are not the primary issue. From the point of view of an international bank, however, these risks are of crucial importance and must be taken into account by the Board in its overall assessment of the resulting risks and benefits.

If the current UBS Board of Directors were now to initiate lawsuits against former directors and officers, it could be accused of wasting the bank's resources. In addition, the side effects mentioned above would significantly distract UBS and its employees from their day-to-day business for years to come. It would also have a negative impact on the confidence among clients and on the Swiss financial market. The Board is of the firm view that it would be irresponsible to disregard these negative consequences; on the contrary, the best interests of the company demand that the Board refrain from initiating any such claims.

B. Steps against the former directors and officers of UBS under criminal law

The conduct of the management in connection with the financial market crisis and the resulting subprime losses did not give rise to suspicion of criminal conduct either by employees of UBS or by its management. Thus, the question of consequences under criminal law is relevant only in connection with the US cross-border business.

1. Expert report by Bär & Karrer

In the interest of an up-to-date, comprehensive clarification of any possible criminal issues relating to the US cross-border wealth management business, UBS engaged the law firm Bär & Karrer to examine whether, on the basis of the results of the investigations conducted by UBS and the SFBC, sufficient indications were present to suggest that individual employees of UBS may have rendered themselves guilty of conduct punishable under Swiss law.

In the course of its investigation, Bär & Karrer examined, in particular, whether employees of UBS may have rendered themselves culpable under Swiss law if it were assumed that they were involved in conduct by individual US clients (as abettor, accessory or aider) which is punishable under US law. It was further examined whether the conduct of the UBS employees, irrespective of the question of criminal liability under US law, may have rendered them liable under the provisions of Swiss criminal law.

First, Bär & Karrer investigated whether, in the present context, any acts punishable under Swiss criminal tax law were committed by UBS clients. This would have to be the case in order for any contributory act by UBS employees to be punishable under Swiss criminal law. The fact that these acts may conceivably be punishable under applicable US law is irrelevant to an assessment based on Swiss law.

In the second part of the expert report Bär & Karrer analyzed whether UBS employees, in connection with the issues discussed earlier and independently of any possible participation in US tax offenses, had rendered themselves criminally liable under Swiss criminal law. In this context, there were three issues to be examined with a view to the offenses potentially applicable under the Swiss Criminal Code (Strafgesetzbuch, StGB):

- misleading conduct to the prejudice of the American tax authorities in favor of US persons hiding behind companies that held the bank accounts (possibly fraud pursuant to article 146 StGB);
- use of forms containing untrue information as part of the QI System (in particular Form W-8BEN) with the intent to

mislead the American tax authorities (possibly falsification of documents pursuant to article 251 StGB); and

- damaging UBS's assets in breach of professional duty by participating in unlawful acts by bank clients or by the US persons standing behind them, as well as by accepting legal and reputational risks for the bank (possibly criminal malfeasance pursuant to article 158 StGB).

The expert report prepared by Bär & Karrer investigated whether any participation in fraud (article 146 StGB) or any offenses *involving documents* (in particular, falsification of documents pursuant to article 251 subsection 1 StGB) could be excluded in the present context.

Bär & Karrer further assessed whether, on the basis of the facts equally assessed by the SFBC, there were sufficient grounds for a suspicion that UBS employees may have committed acts of criminal malfeasance within the terms of article 158 StGB.

2. Assessment by the public prosecutor's office of the canton of Zurich

The public prosecutor's office responsible for the investigation and prosecution of economic offenses in the canton of Zurich has reached the conclusion that the prerequisite of a sufficient initial suspicion, as required by criminal procedural law for the opening of criminal proceedings, is not satisfied in connection with the US cross-border wealth management business.

In August 2009, the Social Democratic Party of Switzerland filed a criminal complaint with the public prosecutor's office against the persons formerly responsible at UBS. In its complaint, the accusations of criminal malfeasance and aiding and abetting tax evasion were made. On 15 December 2009 the public prosecutor's office of the canton of Zurich announced that it had not been able to establish any initial grounds for suspicion of conduct punishable under Swiss law. For this reason, the public prosecutor's office of the canton of Zurich decided not to open a criminal investigation in this matter.

In response to a query from the Cantonal Council of Zurich as to whether employees of UBS AG could be prosecuted in Switzerland for tax offenses to the detriment of the US, the public prosecutor's office of the canton of Zurich stated that grounds for criminal liability under Swiss law did not exist in this case:

"Acts designed exclusively to frustrate the correct assessment of taxes may, according to the long-standing practice of the Federal Tribunal, at no time be deemed to constitute fraud, within the meaning of article 146 of the Swiss Criminal Code (StGB, SR 311.0) or as falsification of documents, within the meaning of article 251 StGB, regardless of whether the violations at issue are of [Swiss] federal, cantonal or foreign tax law. The infringement of foreign fiscal interests through acts of deception carried out in Switzerland, the exclusive target of which is a foreign tax authority, cannot, therefore, be prosecuted in Switzerland under Swiss criminal law.

Criminal prosecution by Swiss criminal authorities on the basis of foreign criminal tax law fails equally to fall under consideration, even in cases where the acts were committed in Switzerland or by Swiss nationals. Such criminal prosecution would come into consideration only if specific norms for the protection of the foreign tax authority were to exist under Swiss law. Such provisions are not found in the body of Swiss legal norms."

Unofficial translation of the German original of the extract from the minutes of the meeting of the executive council (Regierungsrat) of the Canton of Zurich of 10 June 2009 (KR-Nr. 109/2009)

The public prosecutor's office of the canton of Zurich is, of course, at liberty to commence the criminal proceedings at any time. UBS has to date received no indication that this is to be anticipated.

3. Assessment of the Board of Directors

The evaluation, under Swiss criminal law, of the incidents connected with the US cross-border wealth management business did not produce any indications justifying the commencement of a criminal investigation against any responsible UBS employee. The Board of Directors noted that the public prosecutor's office for economic offenses of the canton of Zurich has reached the same conclusion. The Board of Directors therefore decided not to file a criminal complaint against UBS employees who were responsible at the time.

The Board was supported in its assessment by the conclusions of the investigation by the SFBC, which refrained from filing a criminal complaint due to a lack of sufficient indications of criminal conduct by former corporate bodies or their members.

C. Decision by the Board of Directors

After considering all of the reasons mentioned and weighing all arguments, the Board decided not to take legal action against its former directors and officers and announced the decision to the public on 15 December 2009. The Board of Directors stated the following:

"The investigations show that there are no indications of individual criminal conduct by former senior executives pursuant to Swiss law. There are no indications that they were pursuing personal interests to the detriment of UBS. The Board of Directors has thus decided not to take criminal action. It has also been agreed that no claims before the civil courts relating to directors' and officers' liability or on any other basis will be asserted either.

After careful consideration the Board of Directors has come to the conclusion that many years of uncertainty arising from legal disputes with, at best, an uncertain outcome, and the resulting negative publicity are not in the interest of UBS, its employees, clients and shareholders. By rebuilding a new UBS the Board of Directors has put the past to rest. The new management has already taken extensive and far-reaching measures to ensure that nothing like this can ever happen again."

(Press release of UBS AG on 15 December 2009).

After the shareholders' refusal to grant a discharge for the financial year 2007 at the annual general meeting on 14 April 2010, the Board reviewed the decision of December 2009 again and obtained further legal advice from external experts. These new comprehensive clarifications did not produce any additional findings which would have led to a different conclusion. The Board thus adheres to its original decision not to file claims against former directors and officers.

Therefore, and on the basis of the grounds presented in this report, the Board of Directors is opposed to any attempt by third parties to file actions against former directors and officers or to pursue actions at the company's expense. In the event that individual shareholders were to propose a vote at the general meeting for a resolution in favor of filing a claim at the company's expense, the Board would consider it its duty to recommend that such a proposal be rejected.

V. Where does UBS stand today?

A. Need for a new corporate culture

As set out in Chapter IV, the Board of Directors has decided, after careful consideration, not to take legal steps against former directors and officers of the bank. Even though the question of legal responsibility cannot be completely resolved, the misjudgments, omissions and mistakes of the past years which have been described in detail in this report cannot be ignored. On the basis of the results of the various investigations – and with a view to the extremely critical situation into which UBS maneuvered itself – it must be clearly observed, in retrospect, that the leadership and control structures at UBS were insufficient to adequately address the problems in the subprime and US cross-border wealth management businesses. In addition, fundamental rules of the banking business, such as the execution and enforcement of rules to protect the interests of clients and, ultimately, of the bank, were not observed and implemented with the requisite determination.

UBS has highly qualified employees, a solid client base and a strong brand. When such an organization runs into difficulties, it is normally not the result of one single cause. Rather, it is the combination of several factors, which in concert may draw even a strong corporate giant into difficulties. At the same time, it is difficult to find one simple common denominator for these deficiencies. The investigations did not produce concrete indications that individual persons, through their individual behavior, had intentionally exposed UBS to the risk of severe harm. Even at the peak of the crisis, UBS's staff and management performed their daily business with great commitment. The former top management deserves credit for having taken swift steps to recapitalize the bank and to reduce its risk profile. In addition, a critical analysis of the facts was commissioned and measures to remedy the situations were taken.

The various analyses, opinions and reports that have been summarized in this report nevertheless demonstrate that there were a number of flaws in various areas of the firm which, taken together, contributed to the problems with which UBS was confronted. Not least, corporate cultural factors had facilitated such damaging developments. Some of them are summarized as follows:

- The successful years prior to the crisis may have led some employees to overestimate their own judgment, resist criticism, or even be arrogant, which negatively affected their ability to recognize problematic developments, and to ignore warning signals in some cases.
- The company's leadership sent out the wrong signals: the uncompromising focus throughout the entire bank on

growth and the acquisition of new client money, the ambition to be, at the same time, both the world's largest investment bank and wealth manager, as well as the alignment of the remuneration systems with these objectives, led to a situation in which compliance and control processes were perceived as obstacles to business and were implemented either not at all or only half-heartedly.

- This culture was one of the reasons why critical voices were neither appreciated nor encouraged, and why the prevailing view was that things would revert to normal by themselves in time. This may explain why many measures were implemented hesitantly. The signals sent out from the top were not strong enough to lead to a change in mindset and to a greater focus on sustainability. It is also likely that the lack of control mechanisms may have had the same effect and resulted in what the SFBC Cross-Border Report called a "culture of looking the other way and ignorance" at lower levels.
- Remuneration systems that placed excessive emphasis on the net new money criterion in the cross-border sector, and which excluded risk-allocated costs in connection with financing at the Investment Bank, did not create incentives for sustainable growth.
- Statistical models and ratings had an overriding importance – this may have been caused by the fact that they supported the unquestioned expansion strategy.
- The most important factor in the banking business is always people, whose skills and character are decisive in achieving sustainable profits. The impression is that not all persons at the bank in the past were able to meet the highest standards in this respect.

Based on these considerations, the Board of Directors has come to the conclusion that not only functional and finance market specific but also cultural factors have led to the problems that UBS faced. As a result of this conclusion, today's leadership at UBS is deeply committed to the creation of a new, sustainable corporate culture at UBS.

The new leadership of UBS has done – and continues to do – everything within its power to ensure that the past events do not recur, and to bring UBS back on the track toward long-term success. It is conscious of the importance of the bank not only for its owners, clients and employees, but also for Switzerland and its financial market. It intends to live up to this responsibility.

B. Outlook

A “new UBS”

Since the financial market crisis, the Board of Directors and the Group Executive Board of UBS have undergone a complete renewal process, both in terms of the way they function and with regard to their composition. The powers of both boards are today more clearly defined and separated. The required governance structures have been created in order to steer the bank's business in a consistent manner and to monitor it effectively. Tasks and areas of responsibility have been clearly and authoritatively defined. Long-term succession planning has also been professionalized. The new management was recruited, to a substantial degree, from the outside, and brings with it a comprehensive set of skills and a rich reservoir of experience.

The new leadership places the utmost importance on having UBS and its employees perceived as credible partners. Over the last years, UBS has learned that the satisfaction of its clients, the commitment and loyalty of its employees, the trust of its shareholders and the respect of the authorities, the media and the public are indispensable, and what it means to lose them. A bank will be trusted only if it is financially successful. If it is unable to earn a proper return for its shareholders, there will be no trust in its ability to do so in its client services business. Conversely, every firm – and, in particular, every bank – depends on trust for its success.

For this reason, the new leadership, in determining its strategy in 2009, subjected the priorities and activities in all business units as well as the organizational structures to a comprehensive examination and realignment. In addition, it held detailed deliberations on the UBS corporate culture. In doing so, its overriding objective was to create a new UBS capable of sustainable strong performance.

The result of this effort has been the development of strategic plans and initiatives which the company presented and explained to the shareholders and the financial community on the bank's investor day in the fall of 2009.

Business priorities

In the course of its nearly 150-year history, UBS and its predecessor companies have succeeded in establishing a strong position for themselves in various business sectors among clients throughout the entire world. Even during the past years of repeated losses, revenue flows in numerous sectors and markets remained stable. This was so, above all, in the wealth management business. The new strategy provides that these strengths will be built on in the years to come. The following cornerstones show the priorities UBS will be pursuing in the individual business units.

- **Wealth Management:** UBS intends to maintain its position as one of the leading banks in wealth management for private clients. In doing this, it is of utmost importance that the rules and regulations of the individual countries be respected at all

times – and without exception. To this end, UBS has issued internal guidelines and instructions. The cross-border wealth management business has been realigned. Bank units abroad will be further expanded. Client advisory and support services take into account the fact that client needs have changed, due, in particular, also to the experiences of the financial market crisis.

- **Investment Bank:** The business model and monitoring structures in the UBS Investment Bank have undergone a comprehensive revision. Its business units now closely coordinate with each other and are closely monitored. The focus of business in the Investment Bank is clearly directed toward advisory and client services, and proprietary trading has, accordingly, been drastically reduced. This has also made it possible to reduce the balance sheet, which is today more actively managed. This has created the necessary conditions for UBS to establish a strong position in investment banking in the future as well – with a long-term lower risk profile.
- **Asset Management:** In institutional asset management, UBS has implemented various initiatives for ensuring that a consistently high level of investment performance is achieved. Internal cooperation with the bank's wealth management divisions and the Investment Bank has been intensified and institutionalized, in order to provide clients with a wide offering and thus also a maximum of added value. Thanks to these measures, the asset management business should continue to be an important source of earnings for UBS also in the years to come.
- **Regions:** In the domestic Swiss market, UBS intends to maintain and further strengthen its number one position for private, corporate and institutional clients. Asia remains decisive as a growth market for all business units. More specifically, substantial means will be invested for the further expansion of wealth management in the Asia-Pacific region. In the cross-border business with high net worth clients, the primary emphasis is on growth in the Middle East, in Latin America, and in Central and Eastern Europe, while the focus in Western Europe is on the strengthening of onshore business in local bank units. In its US onshore wealth management, UBS plans to be more selective in the future and to concentrate on the very high net worth clients. The US continues to have great importance also for the Investment Bank.

Robust structures

It is precisely in such globally active enterprises as UBS that there must be a guarantee that corporate leadership is aware at all times of all opportunities and risks that may arise from the company's business activities, and that it is able to take the correct measures and guide the company on a sustainable path. Robust, comprehensive structures are decisive in order to be able to work successfully in the long term throughout all of the company's business units.

With its revamped Corporate Center, UBS has established for itself a strong and reliable backbone. In the course of 2009, all financial and risk control functions, as well as the infrastructure and internal service functions of the entire UBS group have been centralized in this new group-wide shared services division. This has created ideal conditions for effectively supporting management in its tasks of managing and supervising the entire UBS group.

Strong corporate culture

The initiatives for the improvement of the business model and structures are only a part of the changes that UBS has implemented group-wide. The other part concerns the company's corporate culture and way of doing business. The new leadership is convinced that a bank distinguishes itself not only by the magnitude of its business activities, but also by the clarity and reliability of the advice and services it provides and the irreproachable conduct of its employees.

– *Guiding principles and values:* Within the context of the new corporate culture, the new leadership has defined three strategic guiding principles that all employees must live up to:

Reputation: The bank's reputation is to be treated uncompromisingly as its most valuable asset. This implies honest, law-abiding and responsible behavior on the part of every individual. Such conduct may be expected only of loyal, committed and well-informed employees. For this reason, it is of the utmost importance to corporate management that the quality and contentment of the employees is regularly monitored and supported with the appropriate measures.

Integration: Integration implies, on the one hand, comprehensive, holistic management and control of all important business processes throughout the entire bank. On the other hand, it also implies close cooperation in all internal bank operations in order to provide clients with access to the full expertise on hand in all services offered by the group as a whole. Such conduct is supported by a systematic approach with explicit structures and incentives.

Execution: The banking business is about people. It is for that reason that execution – that is, the manner in which the business is operated, products are offered, and client orders are carried out – is decisive. UBS intends to distinguish itself by the efficiency, seriousness and professionalism of its client relations – and as a bank that acts with transparency, speaks a clear language and keeps its promises.

These guiding principles are supplemented by corporate values that place the ideas of "truth", "clarity" and "performance" at their center. With this, UBS expresses unmistakably the type of conduct that is expected of each and every employee, whether in the bank's internal or external relations.

UBS is aware that financial incentive structures are also a factor in employee conduct. It pays its employees in keeping with market and industry conditions. At the same time, it also takes care that compensation is adequate in relation to the business risks undertaken and serves to motivate sustainable business success. This includes, in certain cases,

the factoring in of a malus component (forfeiture of a portion of the compensation), where violations of internal regulations are discovered or individual performance goals are missed.

– *Code of Conduct and Ethics:* At the beginning of 2010, UBS introduced a new, comprehensive Code of Conduct and Ethics. Compliance therewith is compulsory for all employees, including members of the Board of Directors. The principles and standards described in the code serve as guidelines for all business activities as well as relations with clients, other employees, shareholders, supervisory authorities and business partners. It establishes a personal obligation on the part of every employee to conduct him- or herself appropriately and responsibly, and formulates corresponding rules. The code is a part of all important training measures, so that it is properly understood and correctly implemented. Ignorance of the code, of the applicable laws and regulations, of UBS policies or of best business practices is not accepted as excuse for violations. Where violations occur, various sanctions are provided for, from warnings to cuts in pay and up to and including dismissal.

– *Employee communication:* The new leadership has made its expectations unmistakably clear to the bank's employees. It communicates actively with the employees and seeks dialogue with them.

Employees are expected to take responsibility themselves for the execution of the relevant guiding principles and initiatives in their respective areas and thus also for the transformation of the new UBS. It is incumbent upon them, wherever possible, to actively change or to take up with their superiors anything in their daily work that is in contradiction therewith. They are encouraged to be critical and to act consistently and with discipline within their own areas of responsibility. It is expressly stated that in the new UBS, the objective is not growth per se, but improvement in the performance of one's own job and in finding solutions that make equal sense for both the clients and for the bank.

Globally oriented with its roots in Switzerland

UBS is one of the globally leading wealth managers, is an internationally active investment bank and offers asset management services on a global scale. UBS remains committed to this global orientation.

However, Switzerland plays a special role for UBS, because it is here where the bank has its roots, and because it is firmly positioned here in all of its business units and client segments.

UBS headquarters are located in Switzerland, and over a third of its entire staff, that is, over 23,000 employees, are located here. Swiss political circles, media and the public all show great interest in UBS. UBS intends to strengthen its relationship with all Swiss interest groups, to encourage dialogue and communicate actively. Its purpose thereby is to create understanding for its position and decisions, but, at the same time, also to understand the positions of others.

The fact that UBS participates in discussions about Switzerland's future as a financial center is part of the responsibility it bears toward its clients, its shareholders and its employees all

around the world. At the same time, UBS is aware of its significance for the stability of the Swiss financial system and takes this seriously.

UBS invests considerable sums every year in its Swiss business activities. Currently it is planning to renovate its over 300 branches in the country, the most comprehensive branch modernization undertaking in its history. Support for non-profit organizations and charities is a tradition that continues. UBS is also an active sponsor of cultural and sporting events in Switzerland and contributes to the promotion of young talent.

UBS also plays an important role for Switzerland both as an employer and as a provider of professional training in banking, and it takes its responsibility in this role seriously: in 2010 already nearly 700 new university graduates, over 800 interns and some 300 trainees have been hired.

Roughly 2.5 million private individuals and 135,000 compa-

nies, that is, nearly every second company in the country, have a business relationship with UBS. With a volume of approximately 40 billion Swiss francs, it is one of the largest corporate lenders in the country. It is the leader in Switzerland in capital market issuances, corporate mergers and acquisitions as well as in securities trading. Until now, UBS has raised every year roughly 2.5 billion francs in equity for Swiss companies. With its wide range of activities in all regions of Switzerland, UBS provides a direct service to the Swiss economy.

All of this is an incentive for UBS to reinforce its commitment to Switzerland as its home base and to its local clients here. Above all, however, it represents an obligation to ensure, through its professional performance and responsible conduct, that the trust placed in UBS is never again put to the test to the same extent that it has been recently, but is instead further confirmed and strengthened.

Glossary

Source: certain of the following explanations have been taken from the FINMA report published on 14 September 2009, "Financial market crisis and financial market supervision".

Asset-backed security (ABS)	Security similar to an obligation which is backed by a pool of financial assets (e.g. mortgage or consumer loan receivables). The issuer can use them as security for loans. The investor receives a coupon.
ABS / MBS desk	Business unit within the UBS Investment Bank that dealt with ABS and MBS.
Asset and Liability Committee (ALCO)	Senior-management committee of the UBS group dealing with borrowing limits and financing questions.
Backup Withholding Tax	A US tax required to be withheld at source [withholding tax], currently at the rate of 28 percent, on certain payments in the event that the payee fails to provide the so-called "Withholding Agent" with its US taxpayer identification number or to establish that it is exempt from backup withholding.
Bär & Karrer	Bär & Karrer AG is a Swiss law firm domiciled in Zurich.
Beneficial owner	In German: Wirtschaftlich Berechtigter.
BUC	"Business Unit Control" – UBS organizational unit responsible for risk control prior to the financial market crisis.
CCs	Control Committees of the National Council and the Council of States.
CDO desk	Business unit within UBS Investment Bank that dealt with CDOs.
Chairman's Office	(Former) committee composed of the Chairman and Vice Chairman/Chairmen of the UBS Board of Directors.
Chief Risk Officer (CRO)	Highest ranking risk manager within UBS (at divisional or group level).
Collateralized debt obligation (CDO)	Bond backed by a diversified debt portfolio. As a rule a CDO bond is divided among various tranches with different credit ratings. CDO is also the umbrella term for Collateralized Loan Obligations (CLOs), Collateralized Bond Obligations (CBOs) und Collateralized Swap Obligations (CSOs).
Complaint	Statement of claim by the SEC against UBS of 18 February 2009.
Consent	Acknowledgement by UBS by way of a settlement of the decision by the competent court in the proceedings filed by the SEC as part of the settlement reached with the SEC on 18 February 2009.
Country Paper USA (2004)	A document made available on the intranet to UBS personnel, from 2004 onwards, in which the principles for the correct implementation of the rules applicable to the US cross-border business were set forth.
Country Paper USA (2007)	A revised version of Country Paper USA (2004), made available to UBS personnel from 2007 onwards.
Credit Fixed Income	Business unit within UBS Investment Bank.
Deferred Prosecution Agreement (DPA)	Agreement reached with the DOJ as part of a settlement concluded between UBS AG and the DoJ on 18 February 2009, according to which the DoJ, subject to certain conditions precedent, agreed to defer prosecution of UBS AG for at least 18 months and to waive such prosecution definitively in the event that all obligations under the DPA were fulfilled.
Dillon Read Capital Management (DRCM)	Former independent subsidiary of UBS, that was intended to serve as a platform for alternative investment strategies and was expected, in that context, to develop alternative investment vehicles (hedge funds), in particular for investments in the US mortgage market.
DoJ	United States Department of Justice.
DTT	Double Taxation Treaty.
Federal Reserve (Fed)	Central bank of the USA.
FINMA – Swiss Financial Market Supervisory Authority	As of 1 January 2009, Switzerland's financial market supervisory authority, headquartered in Bern. Its supervisory activities extend to all branches of the finance industry (banks, insurance companies, stock exchanges, securities dealers, collective capital investment schemes, and auditors).
Fixed Income, Rates and Currencies	Business unit within UBS Investment Bank, dealing with fixed income products. The term fixed income products refers to securities that pay a set rate of interest, fixed in advance, or coupon rate (e.g., bonds or other debt securities) and thus are intended to guarantee a consistent rate of interest. Because of price fluctuations, however, the overall return on investments in this category may vary over time.

Foreign Exchange / Cash Collateral Trading (FX/CCT)	Business unit within UBS Investment Bank that was responsible for assuring the liquidity of the UBS business units in all divisions of the UBS group.
FTA	Swiss Federal Tax Administration.
Group Internal Audit (GIA)	UBS internal audit.
Hedge funds	Generic term for investment vehicles that follow non-traditional investment strategies. Hedge funds invest in the global markets using special investment strategies that offer the chance of high returns with corresponding risks. Because they often act in the capital markets as the counterparty in hedging transactions involving derivatives, they have come to be referred to as hedge funds.
Homburger	Homburger AG is a Swiss law firm domiciled in Zurich.
Income notes	Securities which, within the structure of a CDO, are the first to bear the default risk. These notes are assorted with the highest risk, but also yield the highest returns.
IRS	Internal Revenue Service, the US tax authority.
IRS Form W-8BEN	IRS form on which a non-US person certifies that it is the beneficial owner of an item of income for US withholding tax purposes. Form W-8BEN is also used to claim benefits under applicable US income tax treaties.
IRS Form W-9	IRS form on which a US person certifies its taxpayer identification number.
Leverage ratio	The term leverage is used in finance to refer to the use of borrowed funds to optimize return on equity. In connection with the accounting and regulation of financial institutions, the leverage ratio is used to indicate the relationship between a company's equity capital and its debt/adjusted balance sheet total.
Mandatory convertible note	A note is a debt security issued on large commercial loans, normally divided into sub-categories, each with its own conditions attached (interest rate, maturity, etc.). Where the note is issued as a mandatory convertible note, the creditor receives repayment of his loan in the form of shares in the company to which the loan was made.
Mortgage-backed security (MBS)	Security similar to an obligation which is backed by a pool of mortgage receivables (securitized building mortgages). The issuer can use them as security for loans. The investor receives a coupon.
Net New Money	New influx of net assets.
Net revenue	Net revenue (revenue following deduction of expenses incurred in generating the revenue).
Non-recourse loans	Mortgage loans under the terms of which the borrower's liability is limited exclusively to the property on which the mortgage was granted.
Non-Resident Alien (NRA)	Person not subject to US taxes.
Onshore business	Wealth management business conducted by UBS with US clients, in which the client accounts are located in the US and the clients are advised locally in the US.
Origination and underwriting	Business involving the acquisition, bundling and resale of investment products.
Paying Agent	Person that makes payments of dividends, interest or sales proceeds.
Prime mortgage	Mortgages in which the borrower is deemed to have a high level of creditworthiness.
Qualified Intermediary (QI)	Qualified (foreign) financial institution.
Qualified Intermediary Agreement (QI Agreement)	A standardized contract prepared by the IRS, which foreign financial institutions (including foreign banks) may conclude with the IRS. The QI Agreement imposes wide-ranging documentation, reporting and withholding obligations on a foreign financial institution.
Rating agencies	<p>Agencies that measure the creditworthiness of borrowers or investments and rate them accordingly, by assigning them a specific note (e.g., AAA, B+, etc.).</p> <p>Credit rating agencies such as Standard & Poor's classify investment products according to creditworthiness into categories ranging between AAA (highest creditworthiness) and D (bankrupt). The intermediate rating levels (AA+, AA, AA-, A, BBB, BB, B, etc.) provide information on the presumed risk of default. Investments with a creditworthiness of BBB- or higher are designated as high-quality investment products ("investment grade"), and investments with a creditworthiness of BB+ or less as speculative securities ("speculative grade").</p> <p>Other credit rating agencies, such as Moody's and Fitch, use similar measurements. In the interests of simplicity, this report only refers to the rating levels used by Standard & Poor's.</p>

Remediation Plan	"UBS's Write-Downs Arising from the Market Dislocation: Lessons Learned and Remediation", report issued by UBS on 6 June 2008.
Renewal Plan	"UBS Plan for Risk Management & Control Renewal", dated 3 September 2008.
Revised Business Model	The UBS AG business model introduced in 2002, the goal of which was to channel existing business relationships with US clients into asset management agreements and to prohibit contacts with US clients using "US Jurisdictional Means".
SEC Restrictions	Various US statutes and regulations issued on the basis thereof, which restrict the providing of cross-border securities-related services in the US or otherwise using "US Jurisdictional Means".
Securities and Exchange Commission (SEC)	US financial market supervisory authority.
Securitization	Securitization involves the transfer of certain assets by the seller, usually to a special purpose vehicle (SPV), which in turn refinances itself by issuing securities backed by the original assets (see asset-backed security).
Securitized Product Group Proprietary Trading Desk	Business unit within the UBS Investment Bank, which engaged in proprietary investments in structured products.
SFBC UBS Subprime Report	Report by the SFBC, "Subprime Crisis: SFBC Investigation Into the Causes of the Write-downs of UBS AG", issued on 30 September 2008.
SFBC Cross-Border Report	"UBS's cross-border business with private clients in the USA – Report by the SFBC on the implementation of the Qualified Intermediary Agreement and on cross-border services of the UBS AG in the USA", issued on 17 December 2008.
SFBC order	Order issued by the SFBC on 21 December 2008 in the matter of the UBS AG cross-border business with private clients in the US.
SIX Swiss Exchange (SIX)	The SIX Swiss Exchange is Switzerland's stock exchange. As such it runs several trading platforms and is the marketplace for various securities sectors (Swiss stocks, bonds denominated in Swiss francs, etc.). As part of the regulatory duties provided for in the Stock Exchange Act, SIX determines the requirements for meeting and maintaining the listing qualifications.
Special purpose vehicle (SPV)	An SPV is a legally and economically independent vehicle established for a specific purpose. It may, for example, be established as part of a securitization transaction for the purpose of acquiring certain receivables and generating the required funds by issuing securities. The SPV has no access to the assets, so that the receivables acquired serve in their entirety as security for the investors.
StGB	Swiss Criminal Code (Strafgesetzbuch).
Stress test	Analysis of loss potential, intended to provide information as to the earnings and solvency situation of a financial institution in a number of possible scenarios. Stress tests are often carried out by individual institutions as well as by supervisory authorities and central banks.
Subprime	"Subprime" mortgages refer to mortgage loans which are provided to consumers with a low credit rating (borrower quality) or low financial assets.
Subprime securities	Securities for which the underlying consists of loans or mortgages granted to borrowers with limited or insufficient creditworthiness.
Super senior	With regard to asset-backed securities or CDOs, a super senior tranche is a securitization tranche that ranks below a senior tranche (usually AAA rating) in terms of loss absorption. A super senior tranche thus has an even lower default risk than a senior tranche.
Swiss Federal Banking Commission (SFBC)	Former supervisory authority over banks and securities dealers in Switzerland; its functions were assumed by the newly created Swiss Financial Market Supervisory Authority (FINMA), effective 1 January 2009.
Swiss National Bank (SNB)	The central bank of Switzerland, responsible for the Confederation's monetary and currency policies.
UBS	UBS AG.
UBS Shareholder Report	"Shareholder Report on UBS's Write-Downs" issued by UBS on 18 April 2008.
UBS Swiss Financial Advisors AG (UBS SFA AG)	A UBS subsidiary, founded in 2005, which (in contrast to UBS AG) was licensed as a securities dealer in the USA.
UBS Report to the SFBC	"Preliminary Report on UBS's Write-Downs Arising from the Market Dislocation" issued by UBS on 4 April 2008.

US cross-border business	Wealth management business conducted out of Switzerland by UBS AG with US clients who maintained an account relationship with a UBS office located outside the US.
US Jurisdictional Means	Included therein are, for example, all communications to or from the US by means of e-mail, telephone, telefax or the postal service.
Value-at-risk	Statistical measure of risk that is often used in the financial sector to assess possible losses. VaR indicates the loss threshold that a risk position, with a certain degree of probability (confidence level), will not exceed within a given time horizon. For example, VaR of 100 million francs for a risk position with a ten-day holding period and a confidence level of 95 percent indicates that there is a 5 percent likelihood of it generating losses greater than 100 million francs over the next ten days.
Wachtell	US law firm Wachtell, Lipton, Rosen & Katz.
Wachtell Report	Report by Wachtell issued on 14 October 2008.
Withholding Agent	Paying Agent with a duty to render account to the IRS concerning income earned on US securities by a person subject to US taxes, in keeping with reporting requirements, stating the identity of the individual taxpayer or his tax identification number.
WM & BB	Wealth Management & Business Banking.



UBS AG
P.O. Box, CH-8098 Zurich
P.O. Box, CH-4002 Basel

www.ubs.com

Federal Reserve (Fed)	Notenbank der USA
Fixed Income, Rates and Currencies	Geschäftseinheit innerhalb der Investmentbank der UBS, die mit Fixed-Income-Produkten arbeitet. Als Fixed-Income-Produkte werden Effekten bezeichnet, die einen im Voraus fest vereinbarten Zinssatz resp. Coupon haben (z.B. Anleihen oder Obligationen) und somit eine konstante Zinshöhe garantieren sollen. Infolge von Kursschwankungen kann sich jedoch die Gesamrendite dieser Investmentkategorie im Zeitverlauf verändern.
«Flow-through»-Gesellschaften	Gesellschaftsstrukturen, bei denen die von diesen Gesellschaften gehaltenen Vermögenswerte für die Zwecke des US-Steuerrechts den dahinterstehenden wirtschaftlich berechtigten Privatpersonen zugerechnet werden.
Foreign Exchange / Cash Collateral Trading (FX/CCT)	Geschäftseinheit innerhalb der Investmentbank der UBS, die für sämtliche Bereiche des UBS-Konzerns für die Sicherstellung der Liquidität der Geschäftseinheiten der UBS zuständig war.
Formular W-8BEN	Ein von Nicht-US-Steuerpflichtigen zu unterzeichnendes Formular, worin diese unter Strafandrohung bestätigen, dass sie selbst der sog. «Beneficial Owner» an den Vermögenswerten auf dem entsprechenden Konto/Depot sind.
Formular W-9	Ein von US-Steuerpflichtigen zu unterzeichnendes Formular, worin diese dem QI ihre US-Steuernummer mitteilen und der Offenlegung ihrer Identität gegenüber dem IRS zustimmen.
GPK	Geschäftsprüfungskommissionen des National- und Ständerates
Group Internal Audit (GIA)	Interne Revision der UBS
Hedge Funds	Oberbegriff für Anlagevehikel, die nichttraditionelle Anlagestrategien verfolgen. Hedge Funds investieren mit speziellen Anlagestrategien an den globalen Märkten und bieten bei entsprechenden Risiken die Chance auf hohe Renditen. Sie stellen oftmals am Kapitalmarkt die Gegenpartei für Absicherungsgeschäfte mittels Derivaten (Hedge), woraus ihre Bezeichnung Hedge Funds abgeleitet worden ist.
Homburger	Homburger AG ist eine schweizerische Anwaltskanzlei mit Sitz in Zürich.
IRS	Internal Revenue Service (US-amerikanische Steuerbehörde)
Länderpapier USA (2004)	Ein den Mitarbeitern der UBS ab 2004 auf dem Intranet zur Verfügung gestelltes Dokument, in dem die Grundsätze für die korrekte Handhabung der anwendbaren Regeln im US-Crossborder-Geschäft festgehalten waren.
Länderpapier USA (2007)	Eine überarbeitete Version des Länderpapiers USA (2004), das den Mitarbeitern der UBS ab 2007 zur Verfügung gestellt wurde.
Mortgage-Backed Securities (MBS)	Obligationsähnliche Wertpapiere, die durch einen Pool von Forderungen aus dem Hypothekarbereich gedeckt sind (verbriefte Immobiliendarlehen). Der Emittent kann sie als Sicherheiten für Kredite einsetzen. Der Investor erhält einen Coupon.
Net New Money	Neugeldzufluss
«Non-flow-through»-Gesellschaften	Gesellschaftsstrukturen, bei denen die von diesen gehaltenen Vermögenswerte für die Zwecke des US-Steuerrechts nicht dem dahinterstehenden wirtschaftlich Berechtigten zugerechnet werden.
Non-Recourse Loans	Hypothekendarlehen, bei dem der Darlehensnehmer ausschliesslich mit dem Grundstück, für das das Darlehen ausgerichtet wurde, haftet.
Non-Resident Alien (NRA)	Nicht US-steuerpflichtige Person
Offshore-Geschäft	Vermögensverwaltungsgeschäft der UBS mit Kunden, bei dem die Konten von einer Niederlassung der UBS ausserhalb des Wohnsitzlandes der Kunden betreut werden.
Onshore-Geschäft	Vermögensverwaltungsgeschäft der UBS mit Kunden, bei dem die Konten von einer Niederlassung der UBS innerhalb des Wohnsitzlandes der Kunden betreut werden.
Origination and Underwriting	Geschäft, das sich mit dem Ankauf, der Bündelung und dem Weiterverkauf von Anlageprodukten befasst.
Pflichtwandelanleihe	Eine Anleihe ist ein Grossdarlehen zugunsten einer Gesellschaft, das in der Regel in Teilbeträge mit einheitlichen Bedingungen (Zinssatz, Laufzeit usw.) aufgeteilt wird. Ist die Anleihe in Form einer Pflichtwandelanleihe ausgestaltet, bekommt der Gläubiger sein Darlehen in Form von Aktien der Gesellschaft zurückbezahlt.

Prime-Hypotheken	Hypotheken, bei denen der Darlehensnehmer mit einer guten Bonität bewertet wird.
Qualified Intermediary (QI)	Qualifiziertes (ausländisches) Finanzinstitut
Qualified Intermediary Agreement (QI Agreement)	Ein vom IRS ausgearbeiteter Standardvertrag, den ausländische Finanzinstitute, insbesondere ausländische Banken, mit dem IRS abschliessen können. Das QI Agreement überbindet den Vertragspartnern des IRS weitreichende Dokumentations-, Melde- und Quellensteuererhebungspflichten.
Qualified Intermediary System (QI-System)	System zur Sicherstellung der ordnungsgemässen Deklaration und Versteuerung von mit US-Wertschriften erzielten Einkünften durch US-Steuerpflichtige und zur Schaffung eines Verfahrens, das es Nicht-US-Steuerpflichtigen ermöglicht, eine Entlastung der von den USA pauschal erhobenen Quellensteuern auf mit US-Wertschriften erzielten Einkünften zu erreichen.
Rating Agencies	<p>Kreditprüfungsagenturen, die Schuldner oder Anlagen aufgrund ihrer Bonität mit bestimmten Noten bewerten (z.B. AAA, B+ usw.).</p> <p>Kreditprüfungsagenturen wie z.B. Standard & Poor's klassieren Anlageprodukte je nach ihrer Bonität zwischen AAA (höchste Bonität) und D (Konkurs) ein. Die Zwischenstufen (AA+, AA, AA-, A, BBB, BB, B usw.) vermitteln einen Aufschluss über das vermutete Ausfallrisiko. Anlagen mit einer Bonität von BBB- oder mehr werden als hochwertige Anlageprodukte («Investment Grade») bezeichnet, Anlagen mit einer Bonität von BB+ oder weniger als Spekulationspapiere («Speculative Grade»).</p> <p>Andere Kreditprüfungsagenturen wie Moody's und Fitch wenden vergleichbare Prüfungen an. Der Einfachheit halber ist im vorliegenden Bericht nur von den Einstufungen die Rede, die Standard & Poor's verwendet.</p>
Remediation Plan	Bericht «UBS's Write-Downs Arising from the Market Dislocation: Lessons Learned and Remediation» der UBS vom 6. Juni 2008
Renewal Plan	«UBS Plan for Risk Management & Control Renewal» vom 3. September 2008
Revised Business Model	Geschäftsmodell der UBS, das im Jahr 2002 eingeführt wurde und darauf abzielte, bestehende Geschäftsbeziehungen mit US-Kunden in Vermögensverwaltungsmandate zu überführen und Kontakte mit US-Kunden unter Verwendung von «US Jurisdictional Means» zu verbieten.
Schweizerische Nationalbank (SNB)	Zentralbank der Schweiz, die die Geld- und Währungspolitik der Eidgenossenschaft führt.
SEC Consent Order	Vergleich vom 18. Februar 2009 zwischen dem DoJ, der SEC und der UBS zur Beilegung der US-amerikanischen Verfahren im Zusammenhang mit dem US-Crossborder-Geschäft
SEC-Restriktionen	Verschiedene US-Gesetze sowie darauf gestützt erlassene Reglemente, welche die grenzüberschreitende Erbringung von Finanzdienstleistungen beschränken.
Securities and Exchange Commission (SEC)	US-amerikanische Finanzmarktaufsichtsbehörde
Securitized Product Group Proprietary Trading Desk	Geschäftseinheit innerhalb der Investmentbank der UBS, die Investitionen in strukturierte Produkte auf eigene Rechnung vornahm.
SIX Swiss Exchange (SIX)	Die SIX Swiss Exchange ist die Schweizer Börse. Als solche betreibt diese mehrere Handelsplattformen und ist Marktplatz für verschiedene Wertpapiersegmente (Schweizer Aktien, Schweizer-Franken-Anleihen usw.). Im Rahmen der im Börsengesetz vorgesehenen regulatorischen Aufgaben bestimmt die SIX die Anforderungen für die Kotierung und deren Aufrechterhaltung.
Special Purpose Vehicle (SPV)	Ein SPV ist eine rechtlich und wirtschaftlich selbständige Zweckgesellschaft. Sie wird beispielsweise dazu gegründet, im Rahmen einer Verbriefungstransaktion bestimmte Forderungen anzukaufen und die erforderliche Refinanzierung über die Emission von Wertpapieren zu generieren. Das SPV hat keinerlei Zugriff auf die Aktiva, so dass die erworbenen Forderungen den Investoren vollständig als Sicherheit dienen.
SSG	Senior Supervisors Group

StGB	Schweizerisches Strafgesetzbuch
Stresstest	Verlustpotenzialanalyse, die über die Einkommens- und Solvenzsituation eines Finanzinstitutes bei möglichen Szenarien Auskunft geben soll. Stresstests werden oft von den einzelnen Instituten wie auch von den Aufsichtsbehörden und den Zentralbanken eingesetzt.
Subprime	Subprime-Hypotheken bezeichnen jene Hypothekarkredite, die an Konsumenten mit geringerer Bonität (Schuldnerqualität) oder finanzieller Kraft vergeben werden.
Subprime-Wertschriften	Effekten, denen Kredite oder Hypotheken für Kreditnehmer mit eingeschränkter oder ungenügender Bonität zugrunde liegen.
Super-Senior	Als Super-Senior bezeichnet man bei Asset-Backed Securities oder CDOs eine Verbriefungstranche, die hinsichtlich der Verlustübernahme nachrangig zur Senior-Tranche (meistens AAA-Rating) steht. Die Super-Senior-Tranche besitzt daher ein noch geringeres Ausfallrisiko als die Senior-Tranche.
UBS	UBS AG
UBS Financial Advisors AG (UBS SFA AG)	Eine im Jahr 2005 gegründete Tochtergesellschaft der UBS, die (im Gegensatz zur UBS) über eine Bewilligung als Wertschriftenhändlerin in den USA verfügte.
UBS Shareholder Report	Bericht «Shareholder Report on UBS's Write-Downs» der UBS vom 18. April 2008
UBS-Bericht an die EBK	Bericht «Preliminary Report on UBS's Write-Downs Arising from the Market Dislocation» der UBS vom 4. April 2008
Umstrukturierungen – Switches	Zwischen die Bank und den US-Steuerpflichtigen, der bisher Vertragspartner der Bank war, wird eine nicht in den USA domizilierte Gesellschaft (häufig eine Offshore-Sitzgesellschaft) geschaltet, wobei der bisherige Kontoinhaber an den von der dazwischengeschobenen Gesellschaft gehaltenen Vermögenswerten aber direkt oder indirekt wirtschaftlich berechtigt bleibt.
Umstrukturierungen – Upgrades	Umgestaltung einer Gesellschaftsstruktur (z.B. Rechtskleidwechsel oder Dazwischenschalten einer Offshore-Sitzgesellschaft), damit die steuerliche Eigenständigkeit der gewählten Struktur anerkannt wird und die von dieser Struktur gehaltenen Vermögenswerte nicht dem dahinterstehenden wirtschaftlich Berechtigten zugerechnet werden können.
US-Crossborder-Geschäft	Vermögensverwaltungsgeschäft der UBS mit US-Kunden, die bei einer Geschäftsstelle der UBS ausserhalb der USA eine Kontobeziehung unterhielten.
US Jurisdictional Means	Darunter fällt beispielsweise jegliche Kommunikation in die USA unter Verwendung von E-Mail, Telefon, Telefax oder Post.
Value-at-Risk	Statistisches Risikomass, das in der Finanzbranche oft zur Beurteilung möglicher Verluste verwendet wird. Der VaR gibt den Verlust an, der eine Risikoposition innerhalb eines bestimmten Zeithorizontes mit einer bestimmten Sicherheitswahrscheinlichkeit (Konfidenzniveau) nicht überschreitet. Beispielsweise bedeutet ein VaR von CHF 100 Millionen bei einer Haltedauer von zehn Tagen sowie einem Konfidenzniveau von 95%, dass der mögliche Verlust der Risikoposition in den nächsten zehn Tagen mit einer Wahrscheinlichkeit von 5% CHF 100 Millionen überschreitet.
Verbriefung	Für eine Verbriefung überträgt der Verkäufer bestimmte Vermögensgegenstände in der Regel auf eine Zweckgesellschaft (SPV), die sich wiederum durch die Ausgabe von mit den ursprünglichen Vermögensgegenständen besicherten Effekten refinanziert (siehe Asset-Backed Securities).
Wachtell	US-amerikanische Anwaltskanzlei Wachtell, Lipton, Rosen & Katz
Wachtell-Bericht	Bericht von Wachtell vom 14. Oktober 2008
Withholding Agent	Zahlstelle, die gegenüber dem IRS über die von einer US-steuerpflichtigen Person mit US-Wertschriften erzielten Einkünfte in einem Meldeverfahren unter Angabe der Identität des betreffenden Steuerpflichtigen bzw. von dessen Steuer-Identifikationsnummer abzurechnen hat.
Zahlstelle	Stelle, welche die Auszahlung von Dividenden auf Aktien oder Zinsen auf Obligationen amerikanischer Unternehmen vornimmt.



UBS AG
Postfach, CH-8098 Zürich
Postfach, CH-4002 Basel

www.ubs.com