

10 February 2009

UBS's compensation decisions

- **UBS's Board of Directors and its Group Executive Board won't receive variable compensation for 2008.**
- **Some former members of the Board and the GEB partially repaid past compensation.**
- **UBS cut overall annual personnel expense by CHF 9.2 billion or 36%, in 2008**
- **Overall variable compensation was reduced by CHF 7.8 billion.**
- **No competitor reduced variable compensation so substantially.**
- **Variable compensation allocated by management was reduced by 85%, to CHF 1.161 billion.**
- **Global Wealth Management and Business Banking received 60% of this pool.**
- **For 2008, a Conditional Variable Compensation Plan was introduced for senior employees to align their interests with those of shareholders and link compensation to UBS's future success.**
- **Similar to previous years, UBS will allocate stock appreciation rights to key position holders.**

1. Introduction

A fundamental reality is that the commitment and contribution of UBS's employees are essential to returning UBS to profitability. Our ability to compensate employees in an appropriate manner relative to competitors, i.e., to retain and attract critical staff, is vital if we are to master the challenges ahead. Our compensation decisions for 2008, which balance these considerations and the requirement to protect UBS's capital base, are in the best interest of UBS's shareholders.

The nature of UBS's compensation model enables the firm to reduce total compensation costs swiftly and substantially while setting a floor on how deeply variable compensation can and should be cut. Ultimately, UBS believes that its shareholders benefit when the firm has a compensation scheme that permits it to recruit and retain skilled people.

The compensation decisions announced today have been approved by UBS's Swiss regulator FINMA on 4 February 2009. As part of the transaction with the Swiss National Bank and the Swiss Confederation, UBS agreed that FINMA approval is required for its compensation decisions for 2008.

2. Variable compensation allocation for 2008

UBS reduced overall personnel expense by CHF 9.2 billion, or 36%, in 2008, primarily by reducing variable compensation. These figures demonstrate the advantages of a compensation model with fixed and variable components in an industry with extreme earnings volatility. UBS was able to adjust variable compensation costs to a changing market environment. The firm will therefore continue to rely on this model of fixed and variable components.

Table 1: Composition of UBS's total personnel expense

	2007 in million CHF	2008 in million CHF	Change, in %	Change, in million CHF
Total personnel expense	25'515	16'262	-36%	-9'253
- Salary and other non-variable compensation	-13'200	-11'974	-9%	-1'226
- Contractually-owed, revenue based compensation of US WM financial advisors	-2'397	-2'133	-11%	-264
= Effective variable compensation	9'918	2'155	-78%	-7'763
- UBS Pactual contractually agreed variable compensation	-726	-319	-56%	-407
- Other contractual compensation and guaranteed payments	-1'287	-675	-48%	-612
= Discretionary variable compensation	7'905	1'161	-85%	-6'744
<u>Actual P&L impact</u>				
Effective variable compensation	9'918	2'155	-78%	-7'763
- Credit due to accounting change	437	-412		
= P&L impact of effective variable compensation	10'355	1'743	-83%	-8'612

Compensation of US financial advisors is defined as commissions on the revenues they generate from clients. These commissions are contractually determined and owed once revenues are generated. They constitute the largest part of the total compensation of financial advisors. Contractually owed, revenue-based compensation of US WM financial advisors decreased by 11%, in line with the revenue decline.

Effective variable compensation was reduced by nearly 80% to CHF 2.155 billion. Due to an accounting effect of CHF 412 million, the actual net P&L impact of effective variable compensation is CHF 1.743 billion, down 83% from 2007. The restatement of accounts for 2007 and previous years related to IFRS2 resulted in several accounting effects.

A significant proportion of the effective variable compensation pool for 2008 is determined by fixed contractual commitments of CHF 994 million, including CHF 319 million of contractually agreed variable compensation for UBS Pactual. In addition to these fixed commitments, which are cash payments, UBS also granted contractually owed deferred instruments. These deferred instruments will only be paid out in the future if certain vesting conditions are fulfilled and will therefore also be expensed in the future (see also section 4 of this note).

Excluding these items, a pool of CHF 1.161 billion was available for discretionary cash payments. The size of this pool, which represents a substantial reduction of CHF 6.744 billion or 85% compared with 2007, was determined by management. It was determined by calculating the minimum amount needed to provide staff with a critical level of total compensation. In many job profiles, UBS maintained a compensation system with lower fixed compensation and higher variable compensation relative to the market.

The allocation of the compensation pool of CHF 1.161 billion to divisions was defined by divisional business performance, individual performance and seniority level. Global Wealth Management & Business Banking received 60% of the pool, the Investment Bank 15%, Global Asset Management 14% and the Corporate Center 11%. Per employee the pool was cut by 95% in the Investment Bank, 75% in Wealth Management US, 73% in Global Asset Management and 58% in both Global Wealth Management & Business Banking (excluding Wealth Management US) and the Corporate Center.

3. Achieving a stronger alignment of employee interests with shareholders'

In order to begin implementing principles of the new compensation model (e.g., long-term financial performance and compensation at risk) announced on 17 November, UBS has introduced a new forward-looking compensation instrument for senior employees (mainly at the MD, ED and D level) with a pool of approximately CHF 900 million. The Conditional Variable Compensation Plan (**CVCP 2010-2012**) will be granted in Q2 2009 and will vest pro-rata in Q2 2010, Q2 2011 and Q2 2012. The vesting of each tranche of the award depends on the following conditions:

- UBS and the division of the employee are profitable in the year prior to the vesting date of the respective tranche.
- There is no additional capital injection by the Swiss Confederation.
- Employees are with the firm at the time of vesting.

From an accounting point of view, each tranche of the CVCP instrument will be expensed over the vesting period (i.e. from grant date to vesting).

Similar to previous years, UBS will allocate stock appreciation rights to key talents as part of the Key Employee Stock Appreciation Plan (**KESAP**).¹ The plan is targeted at the key talent population and at individuals who distinguish themselves through superior performance that has a substantial impact on current results, as well as those expected to be critical to future performance and the sustainability of the business (overall about 5-10% of staff). The final value of these instruments for our employees is dependent on UBS's future performance; they are an example of compensation at risk.

Awards are granted subject to forfeiture conditions and have a three-year cliff-vesting term. They are set at the money on the date of grant. KESAP is granted from conditional shares and has no negative capital effect during the vesting period. There is dilution if/when the rights are exercised.

4. Valuation of deferred compensation instruments

The figures presented in section 2 of this note provide a full breakdown on how UBS's compensation decisions impact UBS's 2008 financial accounts. As FINMA mentions in its statement ("UBS – Variabel Vergütungen"), a total limit was agreed for all deferred instruments. The final future cost of deferred compensation instruments, such as certain contractually owed awards (as mentioned in section 2) and CVCP and KESAP (described in section 3), cannot be determined today. It depends on whether the vesting conditions are fulfilled and on the future value of UBS's share price (in the case of UBS share price-linked instruments, such as KESAP).

¹ KESAP will replace the Key Employee Stock Option Plan. While UBS consistently utilized stock options within its compensation programs, stock appreciation rights are more effective for treasury management.