Answers to the Questions Submitted by Ethos, Swiss Foundation for Sustainable Development, and Pictet Funds SA to the Board of Directors and the External Auditors of UBS AG

14 February 2008

On 18 December 2007, Ethos, Swiss Foundation for Sustainable Development ("Ethos"), and Pictet Funds SA ("Pictet") requested UBS AG and its external auditors, Ernst & Young AG, to provide answers to questions about the effects of the deterioration of the US residential mortgage market on the business of UBS.

We take this opportunity to address in the first part of this brochure the questions submitted to the Board of Directors in writing. We believe it is appropriate that all of our shareholders are able to consider our answers, and we have therefore decided to publish them ahead of the Extraordinary General Meeting on 27 February 2008, rather than presenting them only during that meeting.

The Board of Directors fully and unequivocally supports a further clarification of the effects of the US mortgage crisis on UBS and the root causes of UBS's large losses in this area, and of what the appropriate corrective measures are.

The Swiss Federal Banking Commission ("SFBC") has already initiated an investigation into the matter. As a first step, UBS is required to prepare a report providing a detailed analysis of the causes, as well as recommendations on how such events can be avoided in the future.

In order to ensure objectivity, two law firms and an external auditing firm will support the UBS internal working group responsible for the report. UBS will submit the report to the SFBC at the end of March 2008, and the SFBC will then continue with the investigation on its own. UBS will inform its shareholders in an appropriate way regarding the report's most important findings.

In the second part of this brochure, you will find the answers Ernst & Young AG provided to the questions Ethos and Pictet submitted to them in their capacity as external statutory and group auditor of UBS.

Table of contents

UBS

Part I:
Answers to the Questions Submitted to UBS AG's Board of Directors

Table of contents

Question 1.1

Which specific measures have been taken by UBS to implement SFBC-RS 06/06 in view of its requirement that there be a risk control function independent from the risk management function?

Financial institutions are required to comply with the Swiss Federal Banking Commission ("**SFBC**") Circular 06/06 of 27 September 2006 (the "**SFBC Circular**") as from 1 January 2008. UBS was involved in the original consultation process before the SFBC Circular was issued and concluded that its existing risk management and control framework substantially complied with the SFBC Circular requirements.

In particular, UBS's Risk Management & Control Principles, which were first published in 2000 and approved in revised form by the Board of Directors (the "**BoD**") in 2005, have always reflected the fundamental principle of separate risk management and risk control responsibility, which is one of the cornerstones of the SFBC Circular.

Principle 1 of the UBS Risk Management & Control Principles – Business Management Accountability

This principle states firmly that business management is responsible for the continuous and active management of all risk exposures. In other words, responsibility for the business entails responsibility for the risks involved in the business.

In the context of market risk and credit risk, which are risks deliberately entered into in order to generate a return, "business management" means those units authorized to enter into business engagements with clients, counterparties and customers. Ultimately, the Business Group CEO is responsible for proposing which business activities the Business Group wishes to undertake, and – subject to any necessary approvals from the independent risk control units – which transactions to execute, which positions to take and how to manage the risks day to day.

Principle 2 of the UBS Risk Management & Control Principles – Independent Risk Control

This principle stipulates that an independent risk control process is implemented when required by the nature of the risks, and that independent risk control functions are responsible for providing an objective check on risk taking activities.

The five key elements of the risk control process are:

- risk identification, through continuous monitoring of the portfolios, by assessing new businesses and complex or unusual transactions, and by reviewing the risk profile in the light of market developments and external events;
- risk measurement of quantifiable risks, using methodologies and models which have been independently verified and approved;
- risk policies to reflect the UBS Risk Management & Control Principles, risk capacity and risk appetite, consistent with evolving business requirements and international best practice;
- risk reporting to stakeholders, and to management at all levels, against the approved risk control framework and, where applicable, limits; and
- risk control through monitoring and enforcement of compliance with the UBS Risk Management & Control Principles, with policies and limits and with regulatory requirements.

There are independent market risk, credit risk, operational risk and compliance functions in all Business Groups. The heads of these functions have independent, functional reporting lines to the Group Chief Credit Officer, Group Head of Market Risk, Group Head of Operational Risk or Group Head of Compliance. This maintains their independence beyond the Business Group level. The heads of the functions also report in line within their Business Group through to the Business Group CEOs.

The Group Chief Credit Officer, Group Head of Market Risk and Group Head of Operational Risk report to the Group Chief Risk Officer, and the Group Head of Compliance reports to the Group General Counsel. The Group Chief Risk Officer and Group General Counsel are members of the Group Executive Board ("**GEB**"), which is led by the Group CEO. All of the preceding are members of the Corporate Center and not of any Business Group.

The independent risk control units are responsible for developing the control frameworks that set the boundaries within which risk management may operate and define the circumstances in which they must seek prior risk control approval for business decisions and the level at which that approval must be given. The frameworks include authorities, policies, measures, limits and qualitative controls that are approved by the senior risk controllers of UBS or the relevant Business Group or, in the case of the most important elements, by the GEB, the Chairman's Office ("**ChO**") or the BoD, in accordance with principles laid out in the Organization Regulations.

The independent risk control units are required to monitor risks continuously, and, in accordance with section 124 of the SFBC Circular, to provide regular risk reports to all levels of management, including quarterly reports to the BoD. As required by section 109 of the SFBC Circular, an annual compliance risk report, which includes a risk based action plan, was provided to the BoD for the first time in February 2008. The independent risk control units and Compliance provide ad hoc reports to the ChO and BoD on request or as necessary, and have the right and responsibility to escalate any concerns to senior management (BoD, ChO, GEB).

Questions 1.2 and 1.3

1.2 What measures have been taken to ensure the management of risks in relation to business linked to the US mortgage crisis? In particular, did the three executive BoD members take decisions relating to the management of these risks in 2006 or 2007? If so, which decisions?

1.3 What measures have been taken to ensure the control of risks in relation to business linked to the US mortgage crisis? In particular, did the three executive BoD members take decisions relating to the control of these risks in 2006 or 2007? If so, which decisions?

In the following sections, we provide an explanation of the role of the most senior bodies of UBS, particularly as they relate to risk management and risk control (part 1), the way our home equity-linked exposures are managed (part 2) and controlled (part 3), and the market developments in mid-2007, their impact on UBS and our responses to them (part 4).

1 Senior bodies of UBS

The most **senior bodies of UBS** are the BoD, the ChO, the GEB and the GEB Risk Sub-Committee ("**GRSC**").

(i) BoD and ChO role

The BoD has, under Swiss Banking Law, no direct operational and executive responsibility but is, essentially, limited to a strategic and supervisory function. In this latter area, the ChO acts as the Risk Committee of the BoD, overseeing on behalf of the BoD the risk profile and implementation of the Risk Management & Control Principles.

The three executive BoD members (two since October 2007) constitute the ChO, which is the senior risk control body of UBS. The Executive Vice Chairman – Risk is a permanent attendee at the GRSC (see (ii) below).

Given their statutory, regulatory and organizational roles and responsibilities, the executive members of the BoD have not made decisions relating to the management of risks arising from US home equity-linked business.

(ii) GEB and GRSC role

The GEB has executive management responsibility for the Group, and is responsible for implementing the risk principles, including approval of core risk policies. It receives regular updates on risk matters from the Group Chief Risk Officer, who is a member of the GEB.

The GRSC is appointed by the GEB to prepare its decisions in the risk area. It identifies risks requiring increased management attention by the GEB and monitors these risks. The GRSC reviews risk control standards, concepts, methodologies and limits and considers individual transactions which are material for the Group where specified in the various control frameworks and limit structures.

The GRSC includes the majority of the GEB members and, additionally, the Group Chief Credit Officer, the Group Head of Market Risk and the Group Treasurer. The Executive Vice Chairman - Risk is a permanent attendee (the "**ChO delegate to the GRSC**") and has a right of veto and escalation.

Risk items that require ChO approval are generally submitted first to the GRSC and / or the GEB for their support.

(iii) Risk decisions by senior bodies

Given their roles and authorities, the senior bodies of UBS have variously initiated or been involved in material risk control decisions and have been kept informed about developments in the market, UBS's risk positions and significant actions taken since the start of the market dislocation in early 2007.

When the market dislocation became acute, special reporting to the ChO and GEB was also instituted and is still in place.

2 Risk management structure

UBS's positions in home equity-linked instruments were managed in 2006 and for the first part of 2007 by two Business Groups – the Investment Bank ("**IB**") and Global Asset Management.

The larger part of our holdings in home equity-linked instruments was managed by the IB. The operating and strategic plans for the IB encompassed a build-up of its fixed income business, including real estate finance (a commercial real estate business) and trading in asset-backed securities ("**ABS**") and mortgage-backed securities ("**MBS**").

Global Asset Management managed the other portion of UBS's positions in home equity-linked instruments through Dillon Read Capital Management ("**DRCM**"). DRCM was created in 2005 with the goal of establishing funds in which third-party investors would participate. DRCM reported to Global Asset Management but was established with staff and positions that originated in the IB.

Initially, DRCM was responsible only for the risk management of positions previously managed by the IB. All the positions were held by the "Controlled Entities" – wholly owned and fully consolidated entities within the UBS Group (including the parent bank which continued to hold some of the positions). The risks and returns on the positions in the Controlled Entities were attributable to the IB, which paid management and performance fees to Global Asset Management. In view of this arrangement involving two Business Groups, the GEB supervised risk management of DRCM, and resolved any differences between DRCM and the IB. DRCM subsequently managed an "Outside Investor Fund" consisting primarily of third-party funds. UBS's exposure to the Outside Investor Fund was limited to its minority interest, and the fund itself was subject to a risk management and control framework consistent with that applied to other funds managed by Global Asset Management.

The positions transferred from direct IB risk management to DRCM risk management (i.e. the positions in the Controlled Entities) included the Mortgage Origination and Servicing Group, the Commercial Real Estate unit and some ABS and MBS trading. The Outside Investor Fund also took positions in home equity-linked products.

The positions managed by the IB and the positions in the Controlled Entities managed by DRCM were subject to aggregate limits, with sub-allocations to the two units, and were reported both separately and in aggregate to senior management.

The major part of the home equity-linked positions held by both the IB and DRCM were highly rated by external rating agencies. These ratings were relied upon by the securitization market and by the industry more broadly.

Various hedging strategies were employed by the IB and DRCM to provide protection against adverse market moves.

In first quarter 2007, DRCM sustained losses on positions in home equity-linked instruments, predominantly in the Controlled Entities (resulting in negative trading revenues of CHF 150 million from DRCM for the quarter), but also in the Outside Investor Fund. An analysis by Group Internal Audit concluded that the losses resulted from a combination of extraordinary market developments, long positions in increasingly illiquid, primarily low-rated, sub-prime securities and short positions that did not substantially offset the losses on the long positions due to differing credit ratings (see question 3). DRCM was also adversely affected by differential price movements between long cash positions and credit default swap hedges, and between different instrument types with the same rating.

The GEB subsequently concluded that operating a proprietary framework outside the IB introduced management and operational complexity and that the relevant portfolios would be more effectively managed within the IB. Accordingly, UBS reintegrated the management of the Controlled Entities into the IB in May 2007. Third party investments in the Outside Investor Fund were redeemed and the fund's positions were also transferred into the IB.

3 Risk control frameworks

As required by the Risk Management & Control Principles – and outlined in our response to question 1.1 – the IB has risk control frameworks covering market risk and credit risk. These frameworks include policies, quantitative controls, qualitative controls and reporting. The ChO approves the key elements of the risk control frameworks, including the principal characteristics of the major risk measures, the most significant limits and their allocation to the Business Groups. The GEB approves key policies.

Under both the market and credit risk control frameworks, risk control authority to approve commitments or exposures is vested in the ChO, which further delegates authority to individuals, the highest authority being delegated to the Executive Vice Chairman – Risk. The authority delegated to any credit risk or market risk control officer depends upon their seniority and experience. The level of approval required for a commitment or exposure increases with its size or potential loss and varies according to the quality of the underlying counterparty or name. A similar hierarchical structure applies to risk management approval authorities.

All home equity-linked positions (including those held at the time in the DRCM Controlled Entities) are covered by one or the other of these frameworks, depending on the nature of the exposures and the purpose for which the positions are held.

Market risk is the risk of loss from adverse movements in market variables. Market variables include: general market risk factors such as interest rates, exchange rates, equity market indices and commodities prices and factors specific to individual names affecting the value of their securities and other obligations in tradable form, and derivatives referenced to those names ('single name exposures'). The market risk framework quantitative controls include:

- global portfolio measures:
  - Value at Risk ("**VaR**"), which is a statistical risk measure accepted by regulators for the determination of regulatory capital for market risks; and
  - stress loss, which is measured daily against scenarios representing the most common types of stress events seen in the past. This global measure is supplemented with targeted scenarios for areas of particular concern or vulnerability, and a limit on potential default risk in our portfolio of tradable securities and related derivatives ("issuer default exposure");
- global concentration limits on exposure to individual general market risk factors, including credit spreads;
- concentration controls on exposure to single names arising from debt and equity instruments in tradable form, including derivatives, linked to those names; and
- 'operational' limits, which are established where risks are considered by risk control to be not fully or adequately covered by the global measures or where risk controllers have specific concerns. They can be expressed in a variety of forms, including nominals, market values or risk sensitivities.

All home equity-linked positions controlled under the IB market risk framework are subject to the global portfolio measures (VaR and stress) and relevant global concentration measures (including general credit spread and single name controls). Some operational limits had been established for real estate-related activities, including limits on sub-prime exposures in some portfolios. There was also a "US real estate stress scenario".

The way risk is expressed in many of our measures (including VaR, stress and global concentration limits) is directly based on or derived from the sensitivity of each instrument to changes in market risk factors and the volatility of those factors – the size of moves seen in normal market conditions or in stressed times in the past. Highly rated home equity-linked instruments, which constitute the vast bulk of the IB's home equity-linked portfolio, had, in the past, exhibited very low price volatility, even in stressed markets, reflecting their low historical rates of default and the fact that they are asset-backed, which was expected to result in high recovery rates even under default. Thus none of the market risk measures anticipated the effects of the extreme market dislocation that emerged in 2007 and the losses that would result.

The market risk control framework does not, for the most part, require transactions within established business lines to be pre-approved, because the positions and exposures which are covered by the market risk framework are liquid, in the sense that a position can be sold (e.g. a security) or an exposure can be hedged (e.g. an interest rate risk). Controls include monitoring and reporting of exposures against portfolio and concentration limits or thresholds and identification of adverse trends in risks, revenues or position turnover. Pre-clearance is required for certain kinds of transactions or if a transaction will lead to a breach of limits.

The positions carried in the DRCM Outside Investor Fund were also subject to a risk management and control framework which included measures consistent with those applied to UBS's own account positions, but the positions carried in this Fund were separately managed and controlled - see part 2 of our response to question 4.1.

Credit risk is the risk of loss from failure by a client or counterparty to meet its contractual obligations to UBS. Credit exposures arise from loans, commitments to lend and contingent commitments, and from derivative transactions with counterparties. The credit risk framework quantitative controls include:

- limits on current and potential future exposure to individual counterparties/clients and counterparty groups; and
- portfolio and sub-portfolio limits and guidelines in a variety of forms (nominal, potential stress loss, tenor), including limits on exposure to all but the best rated countries.

Within the IB credit risk framework there are limits on real estate risks, both commercial and residential, including a limit on sub-prime loans.

Because exposures carried under the credit risk framework are generally illiquid, the controls around most types of commitments involve risk management and risk control pre-approval. Additional pre-approvals – including support by the GRSC – may be required if portfolio or other limits or guidelines are breached. The most senior risk managers and risk controllers and members of the GEB and the ChO have therefore had a detailed view of the largest individual exposures within the major portfolios as well as the overall portfolio position.

During 2006 and 2007, as part of their risk control responsibilities, the GRSC, the GEB and in some cases the ChO considered topics related to real estate exposure under the **market and credit risk** frameworks on a number of occasions. These included review and approval or modification of various real estate-related limit proposals as part of the credit and market risk annual limit reviews for 2006 and 2007, and consideration of interim requests resulting from business changes or developments, including the establishment of the IB Real Estate Finance business (commercial real estate). The senior bodies are also kept informed of limit utilizations and excesses through the risk reporting process.

Additionally, the GRSC has considered specific areas such as the ABS and MBS business (discussed in 2006, as part of a wider review of balance sheet utilization, and again in 2007) and the state of the US housing market (as part of the 2006 review of the market risk stress framework).

4 Recent US home equity market developments and UBS's responses

4.1 US home equity market developments

The past year has seen a sudden collapse in important securities markets, with implications for world credit markets. The frequency of large market risk moves has been exceptional and many of these moves have exceeded those of the past five years. Many experienced market professionals regard this period as perhaps the most difficult since 1929.

The losses sustained by UBS on exposures of this type need to be seen in the context of these market events. By first quarter 2007, when UBS sustained its first losses in the sector (negative trading revenues of CHF 150 million in DRCM), it had become evident that some parts of the market were more risky than the rating of the securities implied. What was not evident at the time, however, was the exceptional combination of events which would follow:

- the extreme rates of delinquency and default and low recovery levels now projected in the market for non-prime mortgages, which imply significant losses even on the highest rated tranches of securitization structures;
- the dramatic widening of credit spreads in such a short time, especially on ABS and MBS products;
- the very high correlation across issues and issuers within instrument classes;
- the decoupling of previously quite well correlated instrument classes (cash versus derivatives and single names versus indices), which on occasions resulted in losses on both asset positions and their hedges;
- the very rapid drying up of liquidity in the US home equity-linked market; and
- the severity and duration of the stressed conditions that prevailed in the second half of 2007 and affected all markets to some extent.

One of the consequences of this market dislocation was that the hedges UBS had in place for some of its highly rated US home equity-linked exposures proved ineffective. Furthermore, UBS had believed that additional protection purchased on some of its holdings of Collateralized Debt Obligations ("**CDOs**") would protect it against price deterioration beyond historical experience for AAA securities. Actual and predicted rates of default in the sub-prime market have, however, increased even beyond historical precedents and thus positions which we – and other market participants – had regarded as partially hedged against market deterioration became open positions which continue to lose value as markets decline further. This includes protection purchased from monoline insurers, some of which may no longer be able to fully meet their obligations as a result of their exposure to the US home equity-linked market.

The developments in the US home equity-linked market occurred at a time when market liquidity was disappearing rapidly and a large number of other market participants were trying to divest similar positions. Markets through which we were intending to exit our unhedged positions also became illiquid – the securitization market effectively closed down and remains closed today.

4.2 Risk management response

When DRCM was closed in early May 2007, the IB CEO and his senior management team supervised the reintegration, aligning each DRCM trading unit with the relevant trading area in the IB.

DRCM's losses in first quarter 2007 arose largely on lower rated tranches of residential MBS, whereas the IB generally had short positions in these rating bands, on which it had recorded gains in the quarter. The IB also had positions in the more senior parts of the capital structure of CDOs, which were highly rated by external rating agencies. In July 2007, there was unprecedented deterioration in market prices and liquidity as a result of the worsening outlook for the sub-prime sector, and IB management became concerned that some of the hedges the IB had in place might not prove effective, particularly as projected default rates on mortgages continued to rise.

Senior management of the IB became actively involved in reviewing and monitoring efforts of trading management to assess the situation, reduce exposures and mitigate risk. In the face of a rapid reduction in market liquidity, at a time when many firms with similar types of exposures were endeavouring to execute similar risk reduction strategies, possible exit routes and hedging opportunities were – and remain – limited.

Home equity-linked instruments were originally marked to market prices, but when the market became illiquid, alternative valuation techniques were adopted. There is no industry standard for the valuation of these instruments and UBS therefore developed its own models for the various classes of assets. As the market has continued to change and the outlook to deteriorate, the assumptions in the models and the data inputs have been adjusted to reflect the more extreme projections for lifetime cumulative losses. The valuations derived from the models have been compared to the limited price data available in markets, which remain highly illiquid.

The write-downs of USD 4.4 billion for third quarter and USD 14.0 billion for fourth quarter 2007 are the result of the ongoing deterioration in the underlying US housing market. By far the largest part of these write-downs relate to super senior positions in CDOs. We have not been able to exit or execute effective hedges for a meaningful portion of our positions. Nevertheless efforts continue to reduce positions and mitigate further losses to the extent possible and to focus on risk management tasks; as noted above, risk management and valuation models for the various classes of exposure have been refined and recalibrated; some sales have been achieved, and some hedges put in place; and the units originally trading the positions have been reorganized to share expertise and maximize risk management efficiency, with new management appointed in some areas.

Since the developments in the US home equity-linked market became acute in third quarter 2007, a number of GEB-level senior management changes have been implemented. These were proposed by the ChO and approved by the BoD in accordance with the Organization Regulations. In addition, there have been management and strategy changes in the IB, and continued focus by management at all levels on home equity-linked instruments.

4.3 Treasury response

UBS's balance sheet leverage (balance sheet total as a multiple of shareholders' equity) had, for some years, been high relative to its peers', largely as a result of the size of its trading inventory. This inventory consisted of predominantly highly rated and very liquid assets, and thus the simple comparison of unadjusted leverage ratios was not considered a cause for concern.

In 2006, the ABS and MBS markets grew rapidly, offering attractive yields – well above the IB's internal cost of funding rate – on highly rated and highly liquid assets. The IB was pursuing a growth strategy which explicitly included the ABS and MBS sector, resulting in a significant build-up of trading inventory.

By early 2007 it was judged that further growth in the balance sheet was not sustainable and that both the balance sheet and regulatory capital usage ("risk-weighted assets") would need to be reduced. Group Treasury had been working on a new funding framework which would increase IB's internal cost of funding and require that the term of the funding be aligned to the liquidity of the assets funded. This would result in some trading businesses becoming less attractive from a risk/return perspective and help achieve the desired reductions.

The new framework was supported by the GRSC and the GEB, and supplementary short-term measures were agreed. The funding framework was approved by the ChO in April 2007, and implementation progressed during 2007 and into 2008.

At the time of their approval of the framework, the members of the ChO expressed their concern about the size of the balance sheet and their expectation that it would not grow further. It was initially agreed that the effectiveness of the short term corrective measures should be monitored before determining whether to freeze IB balance sheet usage at the current level, but a hard limit was imposed in May 2007. The IB risk-weighted assets target was subsequently confirmed as a limit.

4.4 Risk control response

As market developments have unfolded during 2007 and into 2008, the BoD, ChO, GEB and GRSC have been kept informed and have had regular discussions on UBS's exposures and the potential losses. A number of actions have been taken, as outlined below. The senior bodies initiated some of these actions, have been involved in many of the decisions and in some cases have been required to give formal approval.

Special Review By Group Internal Audit

As a result of the losses suffered by DRCM in first quarter 2007, the Group Chief Risk Officer, with the support of the ChO, requested Group Internal Audit to conduct a special analytical review of valuation adjustments in the DRCM home equity-linked books – for further detail see our answer to question 3. A preliminary report of findings was given to the GRSC in April 2007. The Audit Committee reviewed and discussed Group Internal Audit's analysis at its 5 June 2007 meeting and reported the findings of that analysis to the BoD on 28 June 2007.

In Depth Portfolio Reviews

Based on a preliminary report of Group Internal Audit's findings in April 2007, the GRSC instructed the Group Head of Market Risk and the IB Chief Risk Officer to undertake an in-depth, portfolio-by-portfolio review of every trading book of the IB, subsequently including those transferred from DRCM, to further understand the purpose and trading strategies of the businesses, the risks generated, and the adequacy of risk capture and measurement. They were also requested to assess any risk control action that needed to be taken to ensure that the risks were properly controlled. Given the scope of the exercise, the portfolios were prioritized and all high priority reviews were completed in 2007, with the remainder to be completed by the end of second quarter 2008. The ChO, GEB and GRSC have been kept informed of progress.

Action plans to address the issues raised, which include infrastructure changes, will be updated as new findings emerge. It is intended that reviews of this kind will become part of an ongoing process to identify and establish appropriate controls on risks that are not appropriately captured by the standard market risk measures, replacing a more generic annual assessment of risks not captured in VaR .

Special Coordination and Enhanced Reporting

In light of the many information requests received from external stakeholders (including regulators and central banks) and internal senior management (BoD, ChO, GEB), the Group Chief Risk Officer established a team whose role was to ensure efficient and consistent responses and to coordinate enhanced reporting. This team collated a special risk and liquidity report for the ChO and GEB, originally weekly and subsequently every two weeks. It includes updates:

- from the Business on the state of markets and trading portfolios;
- from Risk Control on exposures (both gross values and potential loss) and adjustments to the control framework;
- from Finance on valuation issues; and
- from Legal & Compliance on legal and regulatory matters.

A Treasury section on liquidity, funding and balance sheet has recently been replaced by a separate monthly liquidity report to the ChO and GEB.

Limit Reductions

As the wider US real estate market deteriorated and other markets were affected, the Group Chief Risk Officer, with the support of the GEB, proposed across-the-board reductions in IB market risk limits, reductions in credit limits for higher risk portfolios, and reduced approval authorities within the IB. These were approved by the ChO.

For home equity-linked portfolios which have been put into "work-out", no increase in risk is permitted and every effort is being made by business management to reduce exposure (see 4.2).

Risk Control Frameworks

Despite the significant losses we suffered in 2007, we believe that the high level precepts reflected in our Risk Management & Control Principles were and remain appropriate.

The **credit risk framework** has stood up well so far to the testing conditions in the leveraged loan market. Losses to date have been market value adjustments rather than defaults and are within the range predicted by our stress controls. We have also suffered some losses on counterparties with exposures to home equity markets, but these are within the range we would have expected in stressed conditions of this type.

Aspects of the **market risk control framework** were not adequate to identify the risks being carried and prevent losses in the extreme conditions of the second half of 2007. One symptom was that when markets became highly volatile we experienced "backtesting exceptions" – occasions when the 1-day VaR calculated on positions at the close of one business day is exceeded by the negative trading revenues on those positions on the following business day. When VaR is measured to a 99% confidence level, backtesting exceptions can, in theory, be expected one day in 100. We would expect more frequent exceptions when markets show greater volatility than the historical market data from which our VaR is derived. Nevertheless, the number and size of the exceptions experienced in the second half of 2007 have prompted us to review the way positions are represented in VaR and other aspects of our market risk measures.

We have taken a number of actions to strengthen the framework in response to these events and have accelerated or modified other developments that were already in hand. In particular:

- concentration risk controls have been expanded to encompass gross exposures as well as net exposures, and the leveraged values of structured products as well as their notional, nominal or market values. New thresholds have been introduced to trigger higher level approvals for positions which represent a large percentage of an issue or of trading volume;
- the processes for approving new business initiatives, and transactions which are large, structured or complex or which are sensitive for tax, legal, regulatory or accounting reasons, have been tightened and more detailed rules for triggering escalation have been formulated. A key objective here is to identify at an early stage any potential build up of risks that are not appropriately captured by the risk control framework;
- the IB 'Market Risk Framework' policy has been completely revised and approved by the GEB. The revision incorporates important lessons learned and includes more detailed criteria for assessing liquidity and which activities are considered 'trading';

- the real estate stress scenario has been replaced by a more targeted scenario covering key real estate and asset backed exposures;

- we are working on a more radical revision to our global stress testing approach that will better differentiate between the source of a stress event and its contagion effect. This approach has already been agreed as a concept by the ChO, and will require its formal approval before implementation;

- the 5-year historical time series, from which our VaR measure is derived, was updated out-of-cycle in early September 2007 to capture the increased market volatility seen earlier in the third quarter 2007. Further updates have been made as part of the regular cycle. Shocks applied in our stress scenarios have also been updated; and

- more fundamentally, we are progressively introducing more granular representation of risk positions in our VaR, stress and concentration measures to better capture basis risks (the risk of divergent movements between previously correlated asset classes or instruments).

We are also adjusting the way we assess risk exposure across all types of risk and the capacity we have to carry that risk (the 'earnings-at-risk' framework) in light of the lessons learned in 2007. All changes will be considered by the GRSC, GEB and ChO and any fundamental changes will require BoD approval.

Question 1.4

The "Charter for the Chairman's Office" is dated 27 April 2006 and refers to the SFBC Circular 95/1 dated 14 December 1995. Have measures been taken to adapt the "Charter for the Chairman's Office" subsequent to the issuance of the new Circular on 27 September 2006? Have the responsibilities of the Chairman's Office been adapted?

We believe that the Charter in its current form complies with the requirements of the new SFBC Circular (see also the answer of Ernst & Young AG, our external statutory and group auditor, to question 8 in the Ethos / Pictet questionnaire, in which Ernst & Young AG states that nothing has come to their attention that would suggest that UBS has not implemented the SFBC Circular). The Charter is currently in the process of being amended as part of the regular annual review process. The references to the SFBC regulatory framework will be updated as part of that process. The roles and responsibilities of the members of the Chairman's Office are also part of the regular review process.

Question 2.1 and 2.2

2.1 Did the Chairman's Office delegate to the GEB Risk Sub-Committee exercise his right of veto, as laid down in Article 9, para. 6 of the Organization Regulations, in 2006 or 2007

2.2 In 2006 or 2007, were there any cases of disagreement between the Chairman's Office delegate and the GEB Risk Sub-Committee that have led to a decision in accordance with point 7.4.3 of the Appendix to the Organization Regulations?

The ChO delegate to the GRSC did not veto any transactions during 2006 and 2007. Where he might have considered doing so, the GRSC either concurred with his reservations and rejected a proposal or took note of the reservations and reflected them in the conditions subject to which it gave its support. For the same reasons, there were no occasions where a decision needed to be escalated in accordance with point 7.4.3 of the Appendix to the Organization Regulations.

Throughout the period, the ChO delegate has strongly influenced, and in some cases has stipulated, the conditions upon which transactions and other proposals have been supported by the GRSC. As noted in our response to questions 1.2 and 1.3 (see part 3 of that answer), transactional decisions have, for the most part, related to lending – especially leveraged finance, where the ChO delegate has sought to contain the risk to UBS resulting from pressure on market standards. He has also focused attention on risks in various other portfolios, positions and exposures.

Question 2.3

When and how often, in 2006 or 2007, did the Chairman's Office delegate to the GEB Risk Subcommittee report to the Chairman's Office on the subject of risks?

Formal updates were provided to the ChO by the ChO delegate to the GRSC during the following regularly scheduled meetings:

2006 [9 times]	2007 [9 times]
19.01.06	22.01.07
27.02.06	12.03.07
23.03.06	20.04.07
20.04.06	14.06.07
15.06.06	06.08.07
09.08.06	06.09.07
07.09.06	22.10.07
23.10.06	22.11.07
30.11.06	17.12.07

Additionally, in 2007 there were ad hoc meetings among the members of the ChO on the following occasions, at which time updates were provided by the ChO delegate to the GRSC:

2007 [5 times]
13.07.07
20.08.07
29.08.07
04.09.07
24.09.07

Informal interactions between the members of the ChO occurred on a more frequent basis.

Question 2.4

When and how often, in 2006 or 2007, did the Chairman's Office report to the Board of Directors on the subject of risks?

Formal updates were provided to the BoD by the ChO delegate to the GRSC at the following regularly scheduled meetings.

2006 [7 times]	2007 [7 times]
09.02.06	08.02.07
27.04.06	26.04.07
29.06.06	28.06.07
10.08.06	09.08.07
14.09.06	13.09.07
26.10.06	25.10.07
07.12.06	06.12.07

In addition to the updates at the regularly scheduled BoD meetings, the BoD was updated at the following ad hoc meetings:

2007 [7 times]
13.08.07
06.09.07
28.09.07
14.11.07
26.11.07
02.12.07
09.12.07

Question 3 (Existence of a Special Internal Audit in 2006 and 2007)

In accordance with Article 27 of the Organization Regulations, the Chairman's Office can be asked to order a special internal audit.

3.1 In 2006 or 2007, was Group Internal Audit asked to conduct a special internal audit linked to the US mortgage crisis. If so:

– By the Chairman's Office directly?

– By one or more members of the Board of Directors (via the Chairman's Office)?

– By a member of the GEB (with the Chairman's consent)?

In the first quarter of 2007, the home equity trading book, which was part of the DRCM ABS relative value strategy, incurred losses related to sub-prime trading positions. On 29 March 2007, Group Internal Audit was asked by the Group Chief Risk Officer, supported by the ChO, to perform an analytical review of valuation adjustments made in this book, and assess whether further significant valuation risk existed with respect to sub-prime lending activities of the IB and DRCM.

In the third and fourth quarter 2007, Group Internal Audit was not asked to conduct any special investigation into the developments relating to US home equity-linked instruments as management and control functions were addressing the problems resulting from the crisis. The resources of Group Internal Audit were offered by the ChO to the GEB to support management or control functions if considered appropriate. Support was requested and given to reviewing sub-prime position reconciliations and confirmations for certain transactions.

3.2 If so, on what date was this special internal audit requested? What were its findings?

The audit was requested on 29 March 2007 and the findings were presented to the GEB and BoD in June 2007.

The conclusions of the analytical review were that the write-downs resulted from a combination of extraordinary market developments, long positions in increasingly illiquid, primarily low-rated sub-prime securities and short positions that did not substantially offset the losses incurred on the long positions due to differing credit ratings.

Group Internal Audit's review also highlighted that (i) improvements were required in analyzing, measuring and reporting risks inherent in sub-prime related activities; and (ii) valuation uncertainties in both IB and DRCM portfolios were not sufficiently transparent and inherent risks were not adequately analyzed.

Question 4.1

Were the risk control rules applicable to Dillon Reed Capital Management's business before its reintegration into UBS Investment Bank on May 3, 2007 identical to those of UBS? If not, on which points did they differ?

Introductory remark

DRCM managed investments held in two types of entities:

- UBS owned and consolidated entities – the "Controlled Entities". This activity was conducted on behalf of UBS – specifically the IB – and originated with positions transferred out of the IB. All the entities involved were wholly owned and fully consolidated entities of the UBS Group, including the parent bank itself in which some positions were booked; and

- non-consolidated entities – the "Outside Investor Fund". This activity was conducted on behalf of predominantly third party investors, with a minority co-investment from UBS. All the positions were booked in entities which were not consolidated with UBS.

1 DRCM Controlled Entities

The risk control rules applicable to the DRCM Controlled Entities were in substance identical to those applicable to the IB (see the response to questions 1.2 and 1.3, part 3). The Controlled Entities were fully consolidated for financial reporting and regulatory capital purposes and were therefore subject to the same risk frameworks as applied to equivalent business elsewhere in UBS – specifically the IB. When DRCM was established the overall market risk limits covering the IB and DRCM were increased, in part to accommodate the two separately managed businesses.

The Controlled Entities were intended to provide investment opportunities for a minority of third parties and were therefore intended to operate with a greater degree of autonomy than the IB. Accordingly, there were some modifications to the risk control rules. For example, the approved Controlled Entity market risk limits were not accompanied by lower "released" limits that could be exceeded with risk management and risk control approval, and temporary excesses over approved market risk limits could not be approved for DRCM as they generally could for the IB. With respect to trading positions in securities and related derivatives, in the IB, risk management and risk control approval is given to retain positions, or instructions are given to reduce them, when the positions are already on the books. For DRCM, caps on positions were established in advance to allow DRCM to operate with greater autonomy. In addition, because the activities of the Controlled Entities affected the IB but DRCM was a business unit of Global Asset Management, the GEB retained ultimate risk management approval authority for the principal limits in the framework and for resolving differences between the IB and DRCM in the allocation of any limits.

2 DRCM Outside Investor Fund

The DRCM Outside Investor Fund was risk managed and controlled in a similar way to other funds managed by Global Asset Management. The risks to UBS as investment manager were primarily liability and reputation risks, and the purpose of the risk management and control framework for the Outside Investor Fund was to ensure that it was operated within prudent 'risk parameters' and subject to the 'four eyes principle' in order to mitigate these risks.

Consistent with UBS's Risk Management & Control Principles, DRCM management was responsible for managing the risks taken. This responsibility started with the DRCM Chairman and CEO and was enforced primarily through:

- the Investment Oversight Committee of DRCM, which had to approve the risk parameters, and

- the Risk Administration function, which oversaw the risk in the Outside Investor Fund on a day to day basis on behalf of the DRCM Chairman and CEO and the Investment Oversight Committee.

As for other Global Asset Management funds, the Global Asset Management Chief Risk Officer was responsible for independent risk control for the Outside Investor Fund. He reviewed the risk parameters before they were put in place and monitored compliance on an ongoing basis. He could raise any concerns with the Investment Oversight Committee (at which he had a permanent right of attendance) and with the DRCM Chairman and CEO (with whom he, or his delegate, met on a regular basis) or, if necessary, could escalate issues to the Global Asset Management CEO and the Group Chief Risk Officer, who had intervention rights.

Question 4.2

Did the reintegration of Dillon Reed Capital Management into UBS Investment Bank change the type and the level of risks taken by UBS?

The reintegration of DRCM Controlled Entities into the IB did not change the type or level of risk taken by UBS – all their risks were already carried by UBS. The redemption of the third party investments in the Outside Investor Fund did not change the type of risk taken by UBS, but it did increase the level of risk taken.

On the redemption by UBS of third party investments in the Outside Investor Fund the risks were transferred into IB, resulting in an increase in the IB risk profile on 3 May 2007. The IB VaR limit was temporarily increased, although the increase was not ultimately needed. The UBS VaR limit was not increased and no changes were made to stress or concentration limits to accommodate the new positions.

The integration of the Outside Investor Fund increased portfolio issuer default exposure (a stress measure), increasing a pre-existing excess over the IB limit. Exposure was still above limit at the end of May, but lower than that immediately prior to the integration, as a result of risk reduction measures taken.

The GRSC gave instructions to the business to reduce both issuer default exposure and credit spread exposure (in general and particularly high yield exposure). Exposures were progressively brought down at the instruction of senior management as the markets became more difficult and risky.

Question 5 (Remuneration system for risk control employees)

The SFBC Circular dated September 27, 2006 specifies that the remuneration system for risk control employees must not contain elements which could lead to a conflict of interest.

What were the performance indicators applied to establish the 2006 and 2007 remuneration of risk control employees? Of the Group Chief Risk Officer? Of the Chairman's Office delegate to the GEB Risk Subcommittee?

In 2006, variable individual compensation of risk control employees, including the Group Chief Risk Officer and the ChO delegate to the GRSC, was awarded in line with the general compensation principles of UBS. These principles require management to take into account specific quantitative and qualitative factors, based on certain key performance indicators, in particular individual performance, and performance objectives. It has always been UBS's policy to ensure that remuneration of employees with a risk control function is not dependent on the performance of individual products or transactions. This practice was codified in 2007 ("Compensation for Control Functions Policy Supplement") to provide a reference document for the best practice in operation. The Supplement also includes the governance process according to which annual incentives are approved,

The policies of the Supplement applies to all employees in all Business Groups and regions, including senior management, and is applicable for 2007 remuneration.

The key principles of the policy are as follows:

- Discretionary compensation shall be linked to the overall performance of the Group or Business Group as appropriate. The financial performance of the business line for which control responsibility is exercised shall not be taken into account.
- The final incentive compensation decision shall remain with the appropriate Head of the Control Function.
- Performance standards and metrics requested from outside the Control Function shall be limited to generic group wide standards or otherwise approved by the Group function head.
- Compensation decisions shall generally be confined to processes relating to the relevant business year.

For the Group Chief Risk Officer and the ChO delegate to the GRSC, the 2007 performance indicators to drive variable individual compensation entail the contribution to the longer-term strategic objectives and priorities of the risk control function, the ongoing development and improvement of risk control measures and the management of a balance between growth and return expectations, on the one hand, and risk appetite, one the other. At the core of this is the fulfilment of the individual Performance Management and Measurement (PMM) objectives and Key Performance Indicators (KPIs), which in turn reflect roles and responsibilities. An additional component for driving variable compensation is the achievement of UBS's financial targets.

As a GEB member, the Chief Risk Officer is a participant in the Senior Executive Compensation program. This defines the specification of KPIs, tailored to each individual GEB position, that are directly linked to the compensation decision-making process.

Any incentive award to risk control employees is linked, on the one hand, to their individual performance and, on the other, the financial performance of UBS. Individual performance against KPIs and objectives is rigorously assessed at the end of the performance period.

Question 6 (Remuneration of senior management in 2006)

The remuneration of senior management is determined by various performance criteria.

6.1 Should the 2006 remuneration of senior management be adjusted bearing in mind the risks that have become known in relation to business linked to the US mortgage crisis?

To determine the actual remuneration for senior management, at the beginning of February 2007 the results achieved in 2006 were assessed against the 2006 forecast (UBS and the Business Group financial targets) as well as against similar metrics of competitors. These measurements and assessments resulted in a fixed theoretical amount for performance-related remuneration for each senior executive. This theoretical incentive award was then measured against a number of additional factors: personal performance based on individually defined criteria, additional performance potential, leadership qualities and an executive's contribution to the overall success of UBS. Based on this qualitative assessment, the theoretical incentive was increased or reduced by up to 25%. In February 2007, as a long-term performance incentive, members of senior management were allotted stock options for 2006 in line with their individual performance in the past, their contribution to the overall success of UBS and their future potential. For further details, we refer you to the report on salaries and other remuneration for 2006.

The compensation programs for senior management do not provide for a claw-back mechanism. Compensation programs are part of the benefits payable under the terms of an individual's employment contract and therefore cannot be retroactively changed unilaterally.

However, in order to provide an incentive for long-term value creation, the compensation paid out at senior executive level in any given financial year is closely aligned to the achievement of sustainable profits. Therefore, a substantial portion of the remuneration for senior executives consists of (restricted) UBS shares (at least 50%) and stock options. The guidelines issued by UBS on share ownership by senior executives are amongst the most stringent in the financial sector. All senior executives are required to accumulate and hold five times the average cash element of their overall compensation in the preceding three years in UBS shares after five years in their position. As a result, the value of a substantial portion of a senior executive's personal assets is dependent on the price of UBS shares, and, to this extent, the risks which manifested themselves in 2007 are also reflected in the remuneration paid to executives in 2006.

6.2 If so, by what amount?

We refer you to the explanations given above.

Question 7 (Equal Treatment of Shareholders and Advance Subscription Rights for Mandatory Convertible Notes)

On 10 December 2007, UBS announced various measures to strengthen its capital base in a substantial way.

7.1 Did certain shareholders (for instance Government of Singapore Investment Corporation – GIC) receive information in the days prior to the announcement on 10 December, in particular with regard to the decision of the UBS Board of Directors to propose a capital increase at the upcoming general meeting?

7.2 If so, what information was provided? To whom? When? For what purpose?

On 6 December 2007, at a teleconference with high-ranking representatives of GIC, UBS answered general questions about the structure and timing for the planned transactions, about our valuation models for US sub-prime positions as compared to those of our competitors and about the principal considerations with regard to strengthening our capital base. The answers remained in line with our assessment of the difficult US mortgage market given in the press release of 30 October 2007.

It was known both to GIC and to our investor from the Middle East that the issue of the mandatory convertible notes would require the creation of conditional capital. It was necessary – and therefore justified – to share that information in order to be able to execute the contemplated transaction. However, the decision of the BoD on the capital improvement program, as published on 10 December 2007, was made only after the discussions with the investors had come to an end, on Sunday evening, 9 December 2007.

Comprehensive confidentiality for the discussions with GIC and the investor from the Middle East was ensured by having all those involved sign a secrecy and standstill agreement and by keeping a list of insiders.

7.3 If the subscription rights for convertible bonds were restricted or withdrawn, what would be the legal justification for this?

The shares for the mandatory convertible notes ("**MCNs**") will – subject to approval by the general meeting – be made available from conditional capital. This means that advance subscription rights need to be withdrawn in connection with the capital increase. According to art. 653c para. 2 of the Swiss Code of Obligations, advance subscription rights can be withdrawn for valid reasons. The BoD, when proposing such a withdrawal, must determine whether the withdrawal of the advance subscription rights is in the interests of the company and is necessary to achieve the goal being pursued.

Because of the current situation on the market for US home equity-linked securities, UBS has had to make significant write-downs on the relevant positions. The size of the total loss expected for fourth quarter 2007 and the consequent reduction in the bank's Tier 1 capital ratio could have resulted in a downgrade of our top-tier financial rating, thereby significantly weakening our client and financing position and increasing our financing costs. Furthermore, the value of UBS is crucially dependent on the continuing strength of our client business. The financial market environment, particularly in the United States, is expected to remain unsettled in 2008, and it is therefore essential that UBS is able to manage through this difficult period from a position of financial strength.

We therefore concluded that we needed to strengthen our capital base immediately. A private placement of MCNs with long-term financial investors giving a firm commitment is the most efficient and most certain way of creating core capital in substantial amounts. Only through direct investment by selected major investors giving a firm commitment can such a strengthening of the capital base be achieved. The BoD considered possible alternatives, in particular a public offering of MCNs or a rights offering, but decided not to pursue them for the following reasons:

Public offering of MCNs

MCNs have a complex risk profile and therefore are typically not directed to retail investors. More importantly, a public offering of MCNs would have required the preparation of a prospectus and resulted in an extended delay between its announcement and completion, potentially fuelling further speculation about UBS's capital strength and adversely affecting the development of its Wealth Management business. Therefore, a public offering would not have realized UBS's overriding goal of immediately announcing a firm investment commitment. By contrast, when it announced the capital improvement measures on 10 December 2007, UBS could give a strong statement to the market that CHF 13 billion of new capital had been secured and send a signal of confidence to its client base.

Rights offering

A rights offering is a common way of raising equity, but it would have had a number of drawbacks compared to the issuance of MCNs:

- As stated above, UBS's overriding goal was to announce a firm investment commitment immediately. This would have required a firm underwriting commitment of the rights issue by a banking syndicate, as otherwise there would have been no certainty whether any new equity could be raised at all or in what amount.

- A firm and immediate investment commitment by a banking syndicate at the time of announcement of the capital improvement measures would have required an underwriting commitment prior to the announcement. Since this would have left the announcement risk with the potential banking syndicate, such a procedure would have likely required a substantially higher discount to the market price of the UBS share than the customary level of around 30%. Apart from this, UBS would have likely been forced to accept unfavourable terms and conditions for the underwriting.

- Due to the large expected discount, a substantially higher number of new shares would have had to be issued compared to the MCNs. A CHF13 billion rights offering at a 30-50% discount to the share price immediately prior to announcement of the capital improvement measures would have required between 324.7 and 454.5 million new shares to be issued, compared to a maximum number of new shares of 252.5 million expected to be issued upon conversion of the MCNs.

- A rights offering would have had to be structured as a public offering, requiring not only shareholder approval but also preparation of a prospectus, which would have led to a significant delay. As a result, a public rights offering would have taken a few months to complete. In addition, the banking syndicate underwriting the rights offering would have required adequate compensation for its commitment.

- Market experience shows that the announcement of a rights offering of this size would have led to downward pressure on the share price, and thus would have increased the uncertainty both as to the success of and as to the proceeds to be expected from a rights offering.

Given these considerations, the BoD determined that the issuance of MCNs to two long-term financial investors was in the best interests of UBS and ultimately of its shareholders, and preferable to any other option.

The exclusion of advance subscription rights is therefore justified in our view. It is in the interests of UBS and its shareholders and is appropriate and necessary to achieve the goal of maintaining a robust capital base. In difficult economic times, a robust and attractive capital base is of utmost importance: the trust clients have in a bank's solidity is one of the decisive pillars of success in an asset management business. The BoD considered a rights offering as a way of raising equity with the participation of shareholders. However, weighing up all interests, the BoD decided that, at the current time, it is important and a priority for UBS to strengthen its capital base immediately and firmly. The issue of MCNs, subject to the approval of the general meeting, proved the only viable alternative.

Glossary of certain financial terms

Asset-backed security (ABS)	A debt security the value of which is derived from a pool of assets, or that is collateralized by the cash flows from a pool of assets. An ABS may be backed by loans, leases or other receivables. A security backed by mortgages (commercial or residential) is known as a ***Mortgage-Backed Security*** or MBS.
Backtesting/backtesting exception	A comparison of the 1-day ***Value at Risk*** or VaR calculated on positions at the close of one business day with the actual revenues arising on those positions the next business day. These revenues exclude fees and commissions and revenues from intra-day trading. If actual revenues are negative and exceed the 1-day VaR, a backtesting exception is considered to have occurred.
Balance sheet leverage	Balance sheet total divided by shareholders' equity – a reflection of the extent to which an entity funds itself by borrowing rather than from equity. A simple balance sheet leverage ratio takes no account of the riskiness of the assets funded by borrowing – by contrast, regulatory ratios are risk sensitive (see ***Risk-weighted assets*** and ***Tier 1 capital***).
Basis risk	The risk associated with ***hedging*** one position with an opposite position using instruments that are not perfectly ***correlated***. For example, on the basis of past statistical evidence the prices of two instruments may be expected to move broadly in line with each other and they may therefore be considered to provide a ***hedge*** for each other. Any divergence in price movements between the two – including day to day divergences from the average – will result in gains or losses.
Collateralized debt obligation (CDO)	A structured credit product which is a more complex form of an ***Asset-Backed Security*** (ABS). CDOs are backed by a portfolio of fixed-income assets, e.g. a pool of bonds, loans and other assets, but not all assets are necessarily of the same type (which distinguishes CDOs from other types of ABS). CDOs are structured to offer investors different degrees of risk and correspondingly different levels of income depending on which "tranche" they invest in. These tranches carry different credit ***ratings*** and are grouped into: senior tranches (rated AAA, AA), mezzanine tranches (A to BB), and equity tranches (unrated). Losses on the underlying pool of assets diminish the value of the tranches in order of seniority – holders of the equity tranches lose all their investment before any loss is suffered by the mezzanine holders. The coupon paid to investors is highest on the equity tranches to compensate them for the higher risk.
Concentration limit	A ***limit*** which is intended to prevent excessive exposure to one market risk factor or credit or any group of correlated factors – for example a ***limit*** on exposure to an individual counterparty or counterparty group, or a ***limit*** on exposure to an individual equity market or to general ***credit spreads.***
Correlation	A statistical measure of how two variables move in relation to each other. If two variables are perfectly correlated (either positively or negatively) the change in value of one can be completely predicted from the change in value of the other. Uncorrelated variables move completely independently of each other. If variables are somewhat but not perfectly correlated then ***hedging*** one with the other will create ***basis risk.***

Credit risk	The risk of financial loss resulting from failure by a client or counterparty to meet its contractual obligations under a loan, commitment or derivative transaction.
Credit spread	The difference between the yield on a risk-free debt instrument (e.g., a government bond in domestic currency) and the yield on comparable debt instruments of other – not risk-free – entities. Credit spreads are usually quoted by ***rating*** band, such as AAA or BBB+. The lower the credit ***rating*** is, the higher the yield on the security must be and therefore the wider the credit spread.
Earnings-at-risk	Earnings-at-Risk is an assessment of the potential loss inherent in our business in the current economic cycle, across all business lines, and from all sources, including primary risks, operational risks and business risks. It is measured against a severe, low probability, but nevertheless plausible constellation of events over a one year time horizon.
Hedge	A position taken to offset potential changes in value of another position. The effectiveness of a hedge depends on the ***correlation*** between the factors from which the values of the two positions are derived – the greater the ***correlation***, the more effective the hedge and the less ***basis risk*** is introduced.
Home equity-linked instrument	Any financial instrument the value of which is dependent on or referenced, directly or indirectly, to the performance of residential mortgage borrowers. Depending on the credit quality of the borrower, US residential mortgages are categorized as prime, Alt-A or ***sub-prime***.
Issuer default exposure	Potential loss on the portfolio of ***single name exposures*** resulting from increased default rates such as might be seen during a period of stress.
Leverage	See ***Balance sheet leverage*** ***Leveraged product***
Leveraged product	A financial instrument which is structured so that changes in its value are a multiple of the change in value of the risk factor(s) which drive its value. For example, a CDO equity tranche with a notional amount of USD 10 million which bears the first losses of an underlying pool of assets of USD 100 million is subject to 10 times leverage (see ***Collateralized Debt Obligation***).
Limit	A quantitative control on the amount of exposure that risk managers can take. The limit can be expressed as a volume (total nominal or market value), or a potential loss given specified changes in (an) underlying market variable(s).
Market risk	The risk of financial loss resulting from adverse changes in market variables, including general market risk factors such as interest rates, exchange rates, equity indices, commodity prices and ***credit spreads***, and factors specific to individual names affecting the values of their securities and other obligations in tradable form, and derivatives linked to those names ('***single name exposures***').
Model	A simplified description or representation of an entity or process, property, characteristic or behavior which cannot be represented or predicted with complete certainty. The output of a model is therefore an estimate or approximation.
Mortgage-backed security (MBS)	Debt security similar to an asset-backed security, where the underlying assets are loans to owners of residential or commercial real estate secured with a mortgage over the property.

Rating (external)	Classification by a specialized agency of the credit quality of a corporation, bank, state or special purpose vehicle, or of securities issued by them, essentially expressing probability of default. Financial institutions typically assign their own internal ratings for the assessment of ***credit risk***.
Risk-weighted assets	The total value of an institution's balance sheet assets, off-balance sheet commitments and contingent liabilities and its ***market risk*** positions, measured and risk-weighted according to criteria defined by the Basel Committee for Banking Supervision or a specific regulator (in the case of UBS, the Swiss Federal Banking Commission).
Single name exposure	Exposure to an entity (corporation, financial institution, special purpose entity etc.) or a state or government, arising from holdings of obligations in tradable form (securities, tradable loans), or derivatives, including basket securities, the value of which is wholly or partly linked to the name.
Stress loss	A measure of the potential loss arising from extreme but plausible scenarios, which are used to assess how a portfolio might fare during a period of extreme events in financial markets.
Sub-prime mortgage	A mortgage loan made to a borrower with a poor credit record or low credit score, who is unable to obtain a conventional mortgage because the lender views them as having a higher-than-average risk of default. Sub-prime mortgages generally carry a higher interest rate than conventional mortgages in order to compensate the lender for the higher risk.
Threshold	A level at which an action or approval is required. Unlike a ***limit***, a threshold is not a cap on an exposure or position but rather a trigger point.
Tier 1 capital	The core component of capital which a bank is required to hold to support its risk-taking activities. Tier 1 capital comprises share capital, share premium, retained earnings including current year profit, foreign currency translation differences not recognized in the income statement and hybrid Tier 1 capital (part of equity attributable to minority interests), less accrued expected dividend, net long position in own shares, and goodwill. Tier 1 capital must comprise at least 50% of total regulatory capital and must amount to at least 4% of total risk weighted assets, or more where required by an institution's lead regulator (the SFBC in the case of UBS).
Value at Risk (VaR)	A statistically based portfolio measure of potential loss from adverse movements in market risk factors. VaR is measured to a specified level of confidence (99% in the case of UBS) and there is thus a specified statistical probability (1%) that actual loss could be greater than the VaR estimate. UBS's VaR is based on 5 years of historical market data. For internal ***limit*** and regulatory capital calculations VaR is measured over a 10-day horizon (it assumes positions are held unchanged for 10 days). For ***backtesting***, a 1-day time horizon is used.
Work-out	The process of achieving disposal, restructuring or liquidation of assets which are defaulted or otherwise impaired in order to extract their remaining value cost-effectively and with efficient use of financial and other resources.

List of abbreviations

ABS	Asset-Backed Security
BoD	Board of Directors
CDO	Collateralized Debt Obligations
ChO	Chairman's Office
DRCM	Dillon Read Capital Management
Ethos	Ethos, Swiss Foundation for Sustainable Development
SFBC	Swiss Federal Banking Commission (Eidgenössische Bankenkommission)
SFBC Circular	Circular 06/06 of the Swiss Federal Banking Commission: Supervision and Internal Control, dated 27 September 2006
GEB	Group Executive Board
GRSC	GEB Risk Sub-Committee
IB	Investment Bank
MBS	Mortgage-Backed Security
MCNs	Mandatory Convertible Notes
Pictet	Pictet Funds SA
VaR	Value at Risk

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

www.ubs.com

Part II:
Answers to the Questions Submitted to the External Statutory Auditors / Group Auditors of UBS AG

Table of contents

Introductory remarks by Ernst & Young

As external auditor of UBS AG, Zurich/Basel ("UBS" or the "Bank"), Ernst & Young AG, Basel ("Ernst & Young"), performs numerous audit functions as set out in various laws and regulations and in the articles of association of UBS. The main ones are as follows:

1) As statutory auditor mandated by the Annual General Meeting of Shareholders of UBS, Ernst & Young reports whether in its opinion the accounting records, the annual financial statements approved by the Board of Directors and any proposals for the appropriation of available earnings comply with Swiss law and UBS's articles of association. As group auditor mandated by the Annual General Meeting of Shareholders of UBS, Ernst & Young also reports whether in its opinion the consolidated financial statements comply with Swiss law and the consolidation rules. In both cases, Ernst & Young reports to the General Meeting of Shareholders. Ernst & Young also reports on the internal control over financial reporting in accordance with the standards of the US Public Company Accounting Oversight Board and reports thereon to the General Meeting of Shareholders. Ernst & Young's reports are printed in the Bank's Financial Report and so are publicly available.

2) As auditor of UBS under the banking and stock exchange laws, Ernst & Young audits compliance with the authorization requirements and other audit areas specified by the Swiss Federal Banking Commission ("SFBC") ("regulatory audit"). Ernst & Young informs the Board of Directors and the SFBC of the results of this regulatory audit in a regulatory report, which is confidential and may not be published.

Ernst & Young is likely to complete its audit work in relation to the annual and consolidated financial statements of UBS as at 31 December 2007 on 8 March 2008. The regulatory audit is scheduled for completion in mid-April 2008.

Question 8 (Implementation of the SFBC Circular of 27 September 2006)

What findings have you already made regarding checks on the implementation of the SFBC Circular of 27 September 2006 and communicated to the Board of Directors of UBS AG as appropriate?

Ernst & Young has reviewed the implementation of the provisions of the SFBC Circular of 27 September 2006 entitled "Supervision and Internal Control" ("SFBC Circular 06/6"). Nothing has come to the attention of Ernst & Young that would suggest that the Bank has not implemented SFBC Circular 06/6. Ernst & Young has therefore had no reason to inform the Board of Directors of specific findings in relation to the implementation of SFBC Circular 06/6.

SFBC Circular 06/6 lays down requirements on corporate governance, the supervision of business activities and internal controls, and the supervision thereof by the responsible functions. The institutions concerned were obliged to fulfil these requirements by 1 January 2008 at the latest.

However the majority of the requirements are not new and UBS had largely complied with them prior to 1 January 2007, the date on which SFBC Circular 06/6 came into force. For example, SFBC Circular 06/6 replaced an existing SFBC Circular dated 14 December 1995 on internal audits (SFBC Circular 95/1) and the Swiss Bankers Association guidelines on internal controls of June 2002. Prior to 1 January 2007, UBS was also required to comply with the provisions of the US Sarbanes-Oxley Act, notably with regard to audit committees and internal control over financial reporting.

Question 9 (Any changes to 2006 accounts)

Should the 2006 accounts be restated in view of controls carried out up to the current date, notably in the audit of the 2007 annual accounts?

Ernst & Young interprets this question as relating to any significant errors in the valuation of US sub-prime positions in the 2006 consolidated financial statements of UBS and not to more routine changes required by new or revised accounting standards.

Ernst & Young is likely to complete its audit work in relation to the annual and consolidated financial statements of UBS as at 31 December 2007 on 8 March 2008. In the audit activities that Ernst & Young has performed to date, nothing has come to the attention of Ernst & Young that would suggest that the prior year's consolidated financial statements need to be restated in connection with US sub-prime positions.

The applicable accounting standards require financial instruments in the trading book to be valued at their fair value as at the reporting date. The US sub-prime mortgage market crisis caused a drastic reduction in liquidity during the summer of 2007 in the affected financial instruments; the value adjustments will therefore be booked in the 2007 results. Likewise, if fair value movements – either upward or downward – take place during 2008, these will be booked in the 2008 results.

Question 10 (Independence and adequacy of risk control systems since 2006)

10a) Have you already confirmed or are you otherwise in a position to confirm that the risk control system was independent as at the following dates:
- 31 December 2006?
- 31 December 2007?
- Today (date of Extraordinary General Meeting of Shareholders in mid-February 2008)?

Ernst & Young interprets the question as relating to whether the Bank's risk control function is independent of risk management as required by SFBC Circular 06/6. Ernst & Young can confirm that nothing has come to its attention thus far in the course of the reviews conducted for the 2006 financial year nor for the work undertaken on the 2007 financial year for the regulatory audit (see also Ernst & Young's response to question 8) that would suggest that the risk control function is not independent of risk management as required by SFBC Circular 06/6. Ernst & Young will complete its regulatory audit for the 2007 financial year in mid-April 2008.

Additionally, as mentioned in the introductory remarks, the audit mandate carried out by Ernst & Young has since 2006 included reports on the Bank's internal control over financial reporting as required by the US Public Company Accounting Oversight Board. Although internal control over financial reporting represents only a part of the whole system of internal controls, this does include various provisions in relation to the separation of certain key functions within the Bank. Ernst & Young's report of 10 March 2007 was included in the UBS Financial Report 2006 and expressed a positive opinion without qualifications thereon.

10b) Have you already confirmed or are you otherwise in a position to confirm that the risk control system was appropriate as at the following dates:
- 31 December 2006?
- 31 December 2007?
- Today (date of Extraordinary General Meeting of Shareholders in mid-February 2008)?

Ernst & Young interprets the question as seeking information on Ernst & Young's position in its regulatory reports regarding the adequacy of the Bank's identification, measurement, management and monitoring of risk. Ernst & Young can answer as follows:

2006

In its regulatory report on the 2006 financial year, Ernst & Young raised no qualification regarding the adequacy of the Bank's identification, measurement, management and monitoring of risk. However, as is usual, the report contained comments and recommendations by the internal and external auditors on individual risk control activities, designed to contribute to the ongoing improvement and optimization of processes.

2007 and until today

Ernst & Young will complete its regulatory audit for the 2007 financial year in mid-April 2008, so at this point Ernst & Young cannot comment conclusively on the adequacy of the Bank's identification, measurement, management and monitoring of risk. Ernst & Young's assessment will of course cover the significant losses suffered in connection with the US credit crisis and its findings in this regard as part of its audit activities for the 2007 financial year. Ernst & Young will duly acknowledge the actions taken by the Bank in risk management and control (particularly with regard to the identification, measurement and control of risk and internal risk reporting) in its regulatory report on the 2007 financial year to the Board of Directors and the SFBC.