

# Environmental and Social Risk Policy Framework

Comprehensive, Highest Industry Standards, Deeply Rooted in our Culture

Our **comprehensive environmental and social risk framework is deeply rooted in our culture:**

- it governs client and supplier relationships and applies firm-wide to all activities
- meets the **highest industry standards** as vetted by external auditors and recognized by environmental, social, governance ratings
- is integrated in management practices and control principles and overseen at the **most senior level** of our firm.

This framework is aligned with our [UBS and Society organization](#) that coordinates all our activities and capabilities in sustainable investing (SI) and philanthropy, environmental and human rights policies governing client and supplier relationships, our own environmental footprint, as well as our firm's community investment.

## 1. Introduction

We live in a world that is more interconnected, more interdependent and more interactive than ever before. Rapid technological advances in particular continue to have a profound effect on the economic, political, cultural, environmental and social landscape. These advances have changed the way we think and act. They have altered the way we do business. They have transformed the products and services we consume, and reshaped the perceptions of the world around us. While this has brought with it significant benefits and opportunities, it has also created far greater awareness of the challenges we all face.

As a global company, and the world's largest wealth manager, UBS is in a unique position to help address these challenges, both together with our clients and through our own efforts. Our principles and standards clearly define how we want to do things at UBS. They apply to all aspects of our business and the ways in which we engage with our stakeholders. Our Code of Conduct and Ethics documents our corporate responsibility. Our work in key societal areas such as protecting the environment and respecting human rights are part of this. Living up to our societal responsibilities contributes to the wider goal of sustainable development. As a global firm we take responsibility to lead the debate on important societal topics, contribute to the setting of standards and collaborate in and beyond our industry.

Managing environmental and social risks is a key component of our corporate responsibility. We apply an environmental and social risk policy framework to all our activities. This helps us identify and manage potential adverse impacts to the environment and to human rights, as well as the associated risks affecting our clients and us. We have set standards in product development, investments, financing and for supply chain management decisions. We have identified certain controversial activities we will not engage in, or will only engage in under stringent criteria. As part of this process we engage with clients and suppliers to better understand their processes and policies and to explore how any environmental and social risks may be mitigated. We avoid transactions, products, services, activities or suppliers if there are material environmental and social risks that cannot be properly assessed or mitigated. We will not do business with a counterparty or an issuer who we judge is not addressing environmental or social issues in an appropriate and responsible manner.

The foundation of UBS's environmental and social risk policy framework is established in the [Code of Conduct and Ethics of UBS](#) and the [UBS and Society Policy](#).

## 2. Our focus

Our industry is playing an increasingly active role in addressing global issues such as human rights and the protection of our environment. Climate change impacts ecosystems, societies, and economies worldwide, and we support clients achieving their goals in support of the transition to a low-carbon economy. Growing environmental and human rights concerns have resulted in a fast-changing regulatory and competitive landscape which is affecting our firm, our suppliers and our clients. In response to these emerging risks and opportunities, we are shaping appropriate solutions and commitments.

Twenty-five years ago, UBS was one of the first financial institutions to sign the [United Nations Environment Programme's "Statement by Financial Institutions on the Environment and Sustainable Development"](#). We were also among the first companies to endorse the [UN Global Compact](#), we were an original signatory of the CDP, and our Asset Management business is an Investment Manager signatory to the Principles for Responsible Investment.

In 2000, our firm was a founding member of the [Wolfsberg Group](#) of banks which was originally set up to promote good

practice in combatting money laundering. In 2011, the firm was a driving force behind the establishment of the **Thun Group of Banks**, which has in the meantime published two discussion papers that seek to establish a framework to facilitate the identification of the key challenges and best practice examples for the banking sector's implementation of the UN Guiding Principles on business and human rights. We are a member of the **Roundtable on Sustainable Palm Oil**, and joined its complaints panel in 2014. Also in 2014, we endorsed the Banking Environment Initiative's and Consumer Goods Forum's "**Soft Commodities**" Compact which reaffirms our commitment to developing and implementing responsible business standards.

Our UBS and Society policy is implemented through our global management system. We regularly report on the progress we are making in our annual reporting. This is reviewed and assured externally according to the requirements of the **Global Reporting Initiative's (GRI) Sustainability Reporting Guideline**. UBS is certified according to **ISO 14001**, the international environmental management standard.

### 2.1. Climate change

Climate change is one of the most significant challenges of our time. The world's key environmental and social challenges – such as population growth, energy security, loss of biodiversity and access to drinking water and food – are all closely intertwined with climate change. This makes the transition to a low-carbon economy vital. We support this transition through our comprehensive climate change strategy.

We recognize that this transition will take time and that fossil fuels will be the dominant energy source for some time to come. Nevertheless, we are determined to understand the risks that our clients', and our own, assets are exposed to in the context of uncertain policy and technology developments.

We focus our climate change strategy on risk management, investments, financing, research and our own operations.

We are committed to:

- supporting renewable energy and clean tech transactions;
- not financing new coal-fired power plant projects in high-income OECD countries
- only financing new coal-fired projects outside high-income OECD countries that use high-efficiency, low-emissions technologies
- only supporting other types of transactions of existing coal-fired operators who have a strategy in place to reduce coal dependency or who adhere to strict internationally recognized greenhouse gas emissions standards
- severely restricting lending and capital raising to the coal mining sector and not supporting coal mining companies engaged in MTR operations
- securing 100% of our electricity from renewable sources by 2020, thereby reducing our own greenhouse gas footprint by 75% compared to 2004 levels

We publicly support international, collaborative action against climate change:

- Our Chairman is signatory to the European Financial Services Round Table's statement in support of a strong, ambitious response to climate change.

- Our CEO is a member of the CEO Climate Leaders, an alliance mobilized by the World Economic Forum.
- Our Head Sustainable Investors at Asset Management is member of the FSB Taskforce on Climate-related Financial Disclosures
- We contributed a case study on our climate change stress testing to the Cambridge Institute for Sustainability Leadership's report to the G20 Green Finance Study Group on research challenges and best practices around risk analysis.
- We have joined RE100, a global initiative to get the world's most influential companies to use only renewable power.
- We support the CDP, as an investor member as well as a questionnaire respondent, in their aim to improve company disclosure of risks and opportunities related to natural resources.

For our full climate commitment including key proof points, see "our climate commitment" at [ubs.com/climate](http://ubs.com/climate).

### 2.2. Forests and biodiversity

Deforestation and forest degradation can cause biodiversity to decline. As approximately 80% of the world's documented species are found in tropical rainforests, deforestation will impact global biodiversity. Deforestation is, in fact, second only to the energy sector as a source of global greenhouse gas emissions and accounts for up to 20% of emissions, more than the entire global transport sector.

It is further estimated that more than 50% of tropical deforestation is due to the production of soy, palm oil, timber and beef. In human terms, millions of people rely directly on forests (small-scale agriculture, hunting and gathering, and harvesting forest products such as rubber). Yet, deforestation continues to cause severe societal problems, sometimes leading to violent conflict.

Recognizing these risks, we:

- became member of the **Roundtable on Sustainable Palm Oil** in 2012 and joined its complaints panel in 2014.
- endorsed the Banking Environment Initiative's and Consumer Goods Forum's "**Soft Commodities**" Compact. In doing so, we commit to support the transformation of soft commodity supply chains by expecting producers to be fully certified according to applicable sustainability certification schemes, such as the Roundtable on Sustainable Palm Oil, by 2020. We acknowledge that land acquired without adequate consultation, compensation, and consideration of customary land rights (commonly referred to as land grabbing), can significantly impact local communities: often smallholders who primarily rely on subsistence farming to sustain their livelihood.
- have identified and will not engage in certain activities that contribute to deforestation and its related impacts (sections 3.1 and 3.2).

### 2.3. Human rights

UBS is committed to respecting and promoting human rights in all our business activities. We believe this is a responsible approach underlining our desire to reduce as far as possible potentially negative impacts on society. Our commitment in this important area is long-standing. In July 2000, UBS was one of 43 companies that pledged to adhere to the UN Global

Compact's Principles on human rights, labor standards and the environment.

The principles of the Global Compact, today the largest corporate responsibility initiative globally, stem from the Universal Declaration of Human Rights, the International Labor Organization's Declaration on Fundamental Principles and Rights at Work, the Rio Declaration on Environment and Development and the United Nations Convention Against Corruption. The United Nations took a significant step in 2011 by endorsing the Guiding Principles on Business and Human Rights (UNGPs). At this point, UBS together with other banks decided to jointly consider these developments and conclusions and to share experiences and ideas regarding the implementation of the UNGPs.

To this end, in 2013, UBS co-launched the Thun Group of Banks' first discussion paper on banking and human rights which aims to support banks in mapping and analyzing their own potential adverse impacts in relation to human rights, and also looks at related risks including reputational, legal, operational and financial risks. The Thun Group has since continued its deliberations and the sharing of knowledge and ideas. A second discussion paper, launched in January 2017, explores the meaning and reach of UNGP 13b in a corporate and investment banking context, and provides additional guidance around Principle 17. Both discussion papers are also intended to inform other pertinent initiatives, in the specific case of the second the OECD's proactive agenda on Responsible Business Conduct. UBS is a member of the Advisory Group to the OECD's project.

Recognizing these risks, we:

- established a UBS Position on human rights in 2006. In 2013, we revised the firm's Environmental and Social Risk Framework to formalize accountability for human rights issues.
- stipulated that we will not engage in commercial activities that make use of child labor and forced labor, or that infringe the rights of indigenous peoples (section 3.1).
- will continue our work internally, and externally with the Thun Group of banks and the OECD, to understand how best to implement the UN Guiding Principles across our operations.

### 3. Our standards

UBS has set standards in product development, investments, financing and supply chain management decisions, which include the stipulation of controversial activities and other areas of concern UBS will not engage in, or will only engage in under stringent criteria.

#### 3.1. Controversial Activities – Where UBS will not do business

UBS will not knowingly provide financial or advisory services to corporate clients whose primary business activity, or where the proposed transaction, is associated with severe environmental or social damage to or through use of:

- **World heritage sites** as classified by UNESCO;
- **Wetlands**: on the Ramsar list;

- **Endangered species** of wild flora and fauna listed in Appendix 1 of the Convention on International Trade in Endangered Species;
- **High conservation value forests** as defined by the six categories of the Forestry Stewardship Council (FSC);
- **Illegal fire**: uncontrolled and / or illegal use of fire for land clearance;
- **Illegal logging** including purchase of illegal harvested timber (logs or roundwood);
- **Child labor**: according to ILO-conventions 138 (minimum age) and 182 (worst forms);
- **Forced labor**: according to ILO-convention 29; and
- **Indigenous peoples' rights** in accordance with IFC Performance Standard 7.

The same standards apply when UBS purchases goods or services from suppliers.

In addition, UBS does not directly or indirectly finance the development, production or purchase of controversial weapons of such companies determined to fall within the "Swiss Federal Act on War Materials".

*On the topic of cluster munitions and anti-personnel mines:* UBS does not provide credit facilities to, nor conduct capital market transactions for companies that are involved in the development, production or purchase of cluster munitions and anti-personnel mines. UBS does not include securities of affected companies in its actively-managed retail and institutional funds and in discretionary mandates. UBS draws upon external expertise to decide whether a company is subject to the restrictions imposed by Swiss law.

#### 3.2. Areas of Concern – Where UBS will only do business under stringent criteria

Specific guidelines and escalation criteria apply to transactions with corporate clients engaged in the areas of concern listed below. The guidelines and escalation criteria apply to loans, trade finance, securities and loan underwriting transactions, and investment banking advisory assignments.

Transactions in the areas listed below trigger an enhanced due diligence and approval process. In addition to the assessment of regulatory compliance, adherence to UBS's controversial activities standards, past and present environmental and human rights performance, as well as concerns of stakeholder groups, these transactions require an assessment of the following criteria:

##### 3.2.1. Soft commodities

- **Palm oil**: Companies must be a member of the Roundtable on Sustainable Palm Oil (RSPO), and not subject to any unresolved public criticism from the RSPO. Companies must further have some level of mill or plantation certification and be publicly committed to achieving full certification by 2020 (evidence must be available).
- **Soy**: Companies producing soy in markets at high risk of tropical deforestation must be a member of the Roundtable on Responsible Soy (RTRS), and not subject to any unresolved public criticism from the RTRS. Companies must further be publicly committed to achieving full certification by 2020 (evidence must be available).

- **Timber:** Companies producing timber in markets at high risk of tropical deforestation must seek to achieve full certification of its production by 2020 according to the Forest Stewardship Council (FSC) or a national scheme endorsed against the 2010 Programme for the Endorsement of Forest Certification (PEFC) meta standard for timber products.

### 3.2.2. Power Generation

- **Coal-fired power plants (CFPP):** We do not finance new coal-fired power plant projects in high-income OECD countries. Outside high-income OECD countries, we only finance new coal-fired projects that use high-efficiency, low-emissions (HELE) coal technologies, as defined by the International Energy Agency or the International Finance Corporation. For other types of transactions, we only support companies operating coal-fired power plants if they have a strategy in place to reduce coal dependency or who adhere to strict internationally recognized greenhouse gas emission standards.
- **Large dams:** Transactions directly related to large dams include an assessment against the recommendations made by the World Commission on Dams (WCD) and the International Hydropower Association Sustainability Assessment Protocol.
- **Nuclear power:** Transactions directly related to the construction of new, or upgrading existing nuclear power plants include an assessment on whether the country of domicile of the client / operation has ratified the Treaty on the Non-Proliferation of Nuclear Weapons.

### 3.2.3. Extractives

- **Hydraulic fracturing:** Transactions with companies that practice hydraulic fracturing in environmentally and socially sensitive areas are assessed against their commitment to and certification of voluntary standards, such as the American Petroleum Institute's documents and standards for hydraulic fracturing.
- **Oil sands:** Transactions directly related to oil sand assets (open pit and in situ operations) are assessed against the company's commitment to reducing energy use, greenhouse gas emissions and land footprint, reclamation activities, tailings management, water management and community relationships, as well as commitment to and certification of voluntary standards, e. g. good practice according to the IPIECA-OGP Biodiversity Working Group, the IPIECA Water Management Good Practice Guidelines and membership to industry initiatives such as COSIA and SCI).
- **Arctic drilling:** Transactions involving oil and gas exploration and development in the Arctic are assessed against the company's safety management capacity and track record as well as adequacy of the company's spill response plans.
- **Coal mining:** Since 2010 UBS's overall exposure to coal mining companies has declined markedly. UBS will continue to significantly limit its lending and capital raising engagement with coal mining companies. The firm no longer enters into new lending commitments or raises capital for coal mining companies that are involved in mountain top removal operations. Previous commitments to such firms will be allowed to mature and not extended.

- **Precious metals:** Transactions directly related to precious metals assets that have a controversial environmental and social risk track record are assessed against the client's commitment to and certification of voluntary standards, such as the International Council on Mining & Metals ICMM, ICMC Management Code.
- **Diamonds:** Transactions with companies that mine and trade rough diamonds are assessed on the client's commitment to and certification of voluntary standards, such as the International Council on Mining & Metals ICMM, and rough diamonds must be certified under the Kimberley Process.

## 4. Our processes and governance

UBS applies an environmental and social risk framework to all transactions, products, services and activities such as lending, capital raising, advisory services or investments that involve a party associated with environmentally or socially sensitive activities. The framework seeks to identify and manage potential adverse impacts to the environment and to human rights, as well as the financial and reputation risks of being associated with them.

### 4.1. Integration in risk, compliance and operations processes

Procedures and tools for the identification, assessment and monitoring of environmental and social risks are applied and integrated into standard risk, compliance and operations processes.

- **Client onboarding:** potential clients are assessed for environmental and social risks associated with their business activities as part of UBS's know-your-client compliance processes.
- **Transaction due diligence:** environmental and social risks are identified and assessed as part of standard transaction due diligence and decision making processes in all business divisions and relevant product lines.
- **Product development and investment decision processes:** new financial products and services are reviewed before their launch in order to assess their compatibility and consistency with UBS's environmental and human rights standards. Environmental and social risks are also considered in investment decision processes and when exercising ownership rights like proxy voting and engagement with the management of investee entities.
- **Own operations:** our operational activities and employees, or contractors working on UBS premises, are assessed for compliance with relevant environmental, health and safety, and labor rights regulations.
- **Supply chain management:** environmental and social risks are assessed when selecting and dealing with suppliers. UBS also evaluates goods and services which pose potential environmental, labor and human rights risks during lifecycle (production, usage, and disposal) as part of its purchasing processes.
- **Portfolio review:** at portfolio level, we regularly review sensitive sectors and activities prone to bearing environmental and social risks. We assess client exposure and revenue in such sectors and attempt to benchmark the portfolio quality against regional and or sector averages.

Such portfolio reviews give us an accurate aggregated exposure profile and an enhanced insight into our transaction and client onboarding processes. Based on the outcome of these reviews, we can explore ways to improve the future portfolio profile along a range of risk parameters.

Clients, transactions or suppliers potentially in breach of UBS's position, or otherwise subject to significant environmental and human rights controversies, are identified as part of UBS's

standard risk and compliance processes. Advanced data analytics on companies associated with such risks is integrated into the web-based compliance tool used by our staff before they enter into a client or supplier relationship, or a transaction. The systematic nature of this tool significantly enhances our ability to identify potential risk. In 2016, 2671 referrals were assessed by our environmental and social risk unit, of which 83 were rejected or not pursued, and 258 were approved with qualifications.

### Environmental and social risk assessments

	GRI <sup>1</sup>	For the year ended			% change from
		31.12.16	31.12.15	31.12.14	31.12.15
<b>Cases referred for assessment<sup>2</sup></b>	FS2	2,671	2,192	1,812	22
<b>by region</b>					
Americas	FS2	395	295	354	34
Asia Pacific	FS2	556	520	317	7
Europe, Middle East and Africa	FS2	341	257	297	33
Switzerland	FS2	1,379	1,120	844	23
<b>by business division</b>					
Wealth Management	FS2	429	396	291	8
Wealth Management Americas	FS2	20	20	21	0
Personal & Corporate Banking	FS2	1,226	980	749	25
Asset Management	FS2	2	0	7	
Investment Bank	FS2	971	776	654	25
Corporate Center <sup>3</sup>	FS2	23	20	90	15
<b>by sector</b>					
Metals and mining	FS2	221	217	375	2
Oil and gas	FS2	263	235	357	12
Agribusiness <sup>4</sup>	FS2	330	190	178	74
Utilities	FS2	221	147	89	50
Chemicals	FS2	93	64	56	45
Infrastructure	FS2	88	25	31	252
Other <sup>5</sup>	FS2	1,455	1,314	726	11
<b>by outcome</b>					
approved <sup>6</sup>	FS2	2,304	1,732	1,561	33
approved with qualifications <sup>7</sup>	FS2/FS3	258	373	187	(31)
rejected or not further pursued <sup>8</sup>	FS2	83	87	64	(5)
pending <sup>9</sup>	FS2	26	0	0	

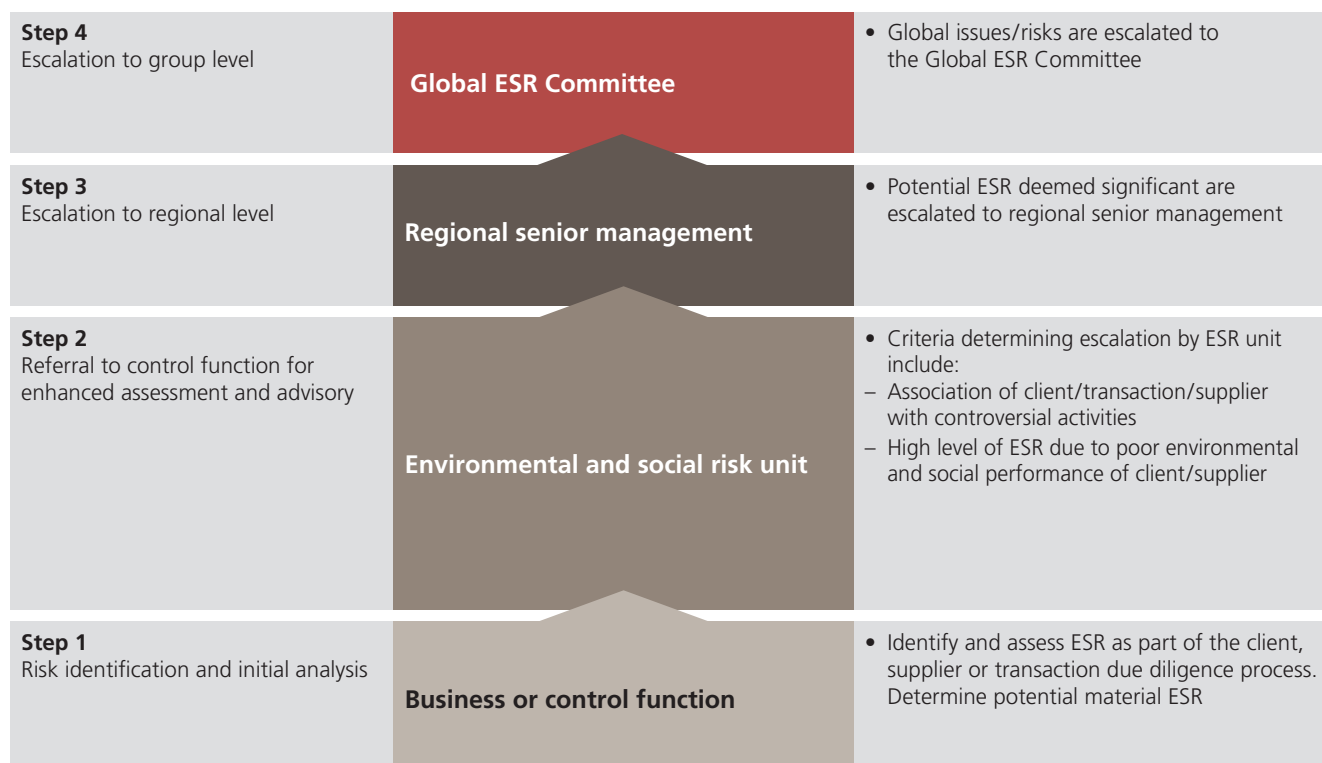
1 Global Reporting Initiative (refer to [www.globalreporting.org](http://www.globalreporting.org)). FS stands for the Performance Indicators defined in the GRI Financial Services Sector Supplement. 2 Transactions and client onboarding requests referred to and assessed by the environmental and social risk (ESR) function. 3 Relates to procurement/sourcing of products and services. 4 Includes e.g. forestry products, biofuels, food and beverage. 5 Include e.g. financial institutions, aerospace and defence, telecom, technology, commodity trading (from 2015). 6 Client/transaction/supplier subject to an ESR assessment and considered in compliance with UBS's ESR framework. 7 Client/transaction/supplier subject to an ESR assessment and approved with qualifications. Qualifications may include ring-fencing of certain assets, conditions towards client / supplier or internal recommendations. 8 Client/transaction/supplier subject to an ESR assessment and rejected or not further pursued. 9 Decision pending. Pending cases 2014/2015 have been closed and reallocated to the other outcome categories.

## 4.2. Escalation and approval processes

Where business or control functions responsible for identifying and assessing environmental and social risks as part of due diligence processes determine the existence of potential

material risks, they refer the client, supplier or transaction to a specialized environmental and social risk unit for enhanced due diligence. If identified risks are believed to pose potentially significant environmental or social risks, they are escalated according to the firm's reputation risk escalation process.

### Environmental and social risk (ESR) escalation process



## 4.3. Governance and oversight

In view of the many environmental and social challenges globally, these topics will continue to increase in relevance for banks. These developments therefore require regular and critical assessment of our policies and practices, based on an accurate monitoring and analysis of societal topics of potential relevance to UBS.

This process is the responsibility of a committee at Group Executive Board-level, the Global Environmental and Social Risk Committee, which sets the overall risk appetite for the firm and resolves transactional and policy matters relating to environmental and social risks and their associated reputation risks.

It is chaired by the Group Chief Risk Officer, who is responsible for the development and implementation of principles and appropriate independent control frameworks for environmental and social risks within UBS.

All corporate responsibility and sustainability developments at UBS are monitored and reviewed by the UBS Corporate Culture and Responsibility Committee, a Board of Director's committee. The Committee supports the Board in its duties to safeguard and advance UBS's reputation for responsible corporate conduct. In this capacity it reviews and monitors the implementation of UBS's ESR framework