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FINANCIAL INDUSTRY REGULATORY AUTHORITY
LETTER OF ACCEPTANCE, WAIVER AND CONSENT
No. 20070095202

TO: Department of Enforcement
Financial Industry Regulatory Authority ("FINRA")

RE: UBS Financial Services, Inc., Respondent, CRD #8174

Pursuant to FINRA Rule 9216 of FINRA's Code of Procedure, Respondent submits this Letter of Acceptance, Waiver and Consent ("AWC") for the purpose of proposing a settlement of the alleged rule violations described below. This AWC is submitted on the condition that, if accepted, FINRA will not bring any future actions against the Firm alleging violations based on the same factual findings described herein.

I.

ACCEPTANCE AND CONSENT

A. Respondent hereby accepts and consents, without admitting or denying the findings, and solely for the purposes of this proceeding and any other proceeding brought by or on behalf of FINRA, or to which FINRA is a party, prior to a hearing and without an adjudication of any issue of law or fact, to the entry of the following findings by FINRA:

BACKGROUND

UBS Financial Services, Inc. ("UBS" or the "Firm"), CRD #8174, has been a registered broker-dealer with FINRA (f/k/a National Association of Securities Dealers or NASD) since October 1936. The Firm is a full service brokerage firm headquartered in Weehawken, New Jersey and has 578 active branch offices with approximately 13,240 registered representatives.

The Firm has the following relevant disciplinary history.

On February 12, 2004, pursuant to Letter of Acceptance, Waiver and Consent No. CAF040007, NASD found that UBS sold shares issued by mutual funds without providing certain customers with the reduction in front-end loads or sales charges, also known as "breakpoint" discounts. NASD censured and fined UBS approximately \$2.3 million and ordered the Firm to undertake certain remedial measures.

On December 20, 2007, pursuant to Letter of Acceptance, Waiver and Consent No. EAF04013000, NASD found that UBS failed to identify certain opportunities for investors to purchase mutual funds at net asset value ("NAV") under NAV transfer programs, failed to provide eligible investors with the benefits of available NAV transfer programs, and failed to establish, maintain and enforce a supervisory system and

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procedures reasonably designed to so. NASD censured and fined UBS \$1 million and ordered the Firm to undertake certain remedial measures.

OVERVIEW

Between January 2004 and December 2005 (the "relevant period"), UBS participated in the sale of 34 initial public offerings ("IPO") of Closed End Funds ("CEFs"). CEFs, including certain of those at issue in this matter, are generally intended for use as long-term investments. Sales charges to the customers who purchased at the time of the initial public offering are built into the offering price of the CEF; in most cases, the market price of the CEFs generally declined after the initial offering.

Despite being aware that CEFs purchased at the initial public offering were most suitable for long-term investments and that the sales charges applied to purchases at the initial public offering made short-term trading of these CEFs generally unsuitable, UBS did not have a system and procedures reasonably designed to detect and prevent unsuitable patterns of short-term trading of CEFs purchased at the initial public offering. As a result, the Firm failed to detect and prevent certain of its registered representatives from engaging in unsuitable short-term trading of CEFs purchased at the initial public offering, which resulted in customer losses of more than \$2 million.

By virtue of the above, UBS violated NASD Rules 3010(a), 3010(b) and 2110.

FACTS AND VIOLATIVE CONDUCT

Background on Closed End Funds

CEFs are investment companies that sell a fixed number of shares in an initial public offering, after which the shares typically trade on a secondary market. The sales charges to the customer are built into the offering price of the CEF purchased at the initial public offering. During the relevant period, the CEFs at issue included a sales load of 4.5%, from which the underwriters' fee and sales concession were paid. The proceeds, after the expenses, were then invested by the CEF based on the investment objectives of the CEF.

The CEFs had a "stabilization period," which was the period of time immediately following the first trading following the initial distribution of the IPO in which the lead underwriter (at least in theory) generally supported the price of the fund. The CEFs' prospectuses noted that the underwriter may purchase common shares to stabilize the fund's price or to reduce short positions, and that this may cause the price of the common shares to be higher than it might otherwise be. Stabilization periods did not exceed 90 days and were generally shorter in duration.

Following the IPO, the price of CEF shares in the secondary market was determined by the market and may have reflected either a premium or a discount of the shares' net asset value ("NAV"). Since expenses to the customer at the time of the IPO were built into the

offering price of the CEF, its initial NAV was always less than the offering price and thus, the market price generally declined after the initial offering.

CEF IPOs also had a penalty bid period, which was the period of time following the initial public offering during which the selling concession paid to the registered representative could be reversed if the shares purchased in the IPO were sold by the customer. The penalty bid period varied from fund to fund, but was generally 30 to 90 days after the initial public offering. It was imposed at the discretion of the lead underwriter.

One regulatory concern relating to CEFs is the potential for registered representatives to earn high fees by soliciting their customers to purchase CEFs at the initial public offering and sell them shortly after the expiration of the penalty bid period, in order to use the proceeds to purchase another CEF at the initial public offering.

UBS's CEF Offerings

During the Relevant Period, UBS participated in the sale of 34 CEF offerings. UBS Securities LLC served as the lead or co-manager in the underwriting of these CEFs and UBS served as a participant in its offerings. These offerings resulted in total sales credits to the Firm of approximately \$185 million. In addition, for certain offerings during the Relevant Period, UBS received a portion of the management and underwriting fees that were paid to UBS Securities LLC. Those payments to the Firm totaled \$25.8 million from management fees and approximately \$9.7 million from underwriting fees each. Generally, the registered representative selling the CEF shares at the initial public offering received a sales concession of 3% of the amount invested, applied to his commission grid or pay-out percentage. UBS offered IPOs of CEFs to its customers on a regular basis and solicited purchases of CEFs. UBS disseminated regular e-mails notifying its registered representatives of the new-issue CEFs and included links to the preliminary prospectus as well as other sales materials. In general, the risk sections of these materials stated that the CEFs were designed for long-term investors and not as a trading vehicle. They also stated that CEFs "frequently trade at a price lower than their net asset value."

UBS Failed To Reasonably Supervise Sales of CEFs

During the relevant period, UBS failed to establish and maintain a system and procedures that were reasonably designed to supervise its registered representatives' sales of new issue CEFs to their customers. Despite being aware that CEFs purchased at the initial public offering were most suitable for long-term investments and that the sales charges applied to purchases at the initial public offering made short-term trading of these CEFs generally unsuitable, the Firm did not have a system and procedures reasonably designed to detect and prevent patterns of unsuitable short-term trading of CEFs purchased at the initial public offering. As a result, the Firm failed to detect and prevent certain of its registered representatives from engaging in unsuitable short-term trading of CEFs purchased at the initial public offering, which resulted in significant losses to customers.

During the relevant period, UBS provided an on-line learning course for managers regarding supervising syndicate activity and issued compliance bulletins on the topic of suitability of certain CEFs. However, the bulletins did not address the issue of short-term trading of syndicate CEFs, but rather discussed suitability requirements for specific CEFs that were offered. Nor did they provide any information about the impact of the sales charges on the NAV and the market price of CEF shares following the initial offering, other than what was provided in the CEF prospectuses that were made available to the Firm's registered representatives.

During the relevant period, the Firm's written procedures did not address short-term trading of CEFs purchased at the initial public offering specifically, and did not provide supervisors with any guidance or warning about the potential abuses and disadvantages relating to short-term trading of CEFs purchased at the initial public offering. Without adequate guidance, branch managers were not on notice that there was any potential problem with short-term sales of CEFs bought at the initial public offering.

Furthermore, UBS did not have an adequate system or procedures to detect short-term trading of CEFs purchased at the initial public offering or whether any of its registered representatives were engaging in a pattern of or in high volumes of short-term trading of CEFs. The only way in which a branch manager would have been able to determine that a specific CEF bought by a customer at the initial public offering was sold shortly after it was purchased was by noting the sale date in the customer's account and trying to match that with a purchase date in the customer's account days, weeks or months earlier, which, according to UBS personnel, required accessing approximately seven different screens in the Firm's computerized system. As such, UBS managers had no practical way to determine how long a CEF had been held by a customer before the sale. In order to detect patterns or high volumes of short-term trading of CEFs purchased at the initial public offering by individual representatives, a branch manager had to review the registered representative's individual customer accounts and check for recurring short-term purchases and sales of CEFs in the accounts.

Certain UBS registered representatives recommended to clients repeated CEF purchases at the initial public offering and subsequent short-term sales without sufficiently considering the effects that the sales charges and other pricing considerations had on their clients' investments. These recommendations were unsuitable and the unsuitable short-term sales of the CEFs resulted in customer losses of more than \$2 million. As a result of the supervisory failures noted above, the Firm was not able to detect and prevent unsuitable short-term trading of CEFs.

By virtue of the above, UBS violated NASD Rules 3010 (a) and (b) and 2110.

OTHER FACTORS

In determining the appropriate sanctions, FINRA considered the following factors: (1) after receiving the results of an SEC examination of one branch office, but prior to FINRA initiating its investigation, UBS engaged outside counsel to conduct a Firm-wide

internal investigation to look into the short-term sales of CEFs purchased at IPO; (2) after conducting an extensive and thorough review, the Firm made extraordinary remediation to customers, some of which was before FINRA initiated its investigation; and (3) the Firm identified the causes of the violations and, before the completion of FINRA's investigation, corrected its systems and procedures and took other steps to prevent future violations.

Specifically, following completion of the review, the Firm instituted a new training requirement on CEFs, instituted a new system component to detect and prevent unsuitable short-term sales of CEFs, and updated its written procedures to address CEF issues. In addition, following its review, UBS sanctioned 17 registered representatives still at the Firm, who the Firm found to have made unsuitable CEF recommendations.

With regard to remediation, by February 2008, the Firm paid in excess of \$2 million in remediation to approximately 189 accounts, which constitutes all of the customers of the registered representatives it sanctioned and those registered representatives who had resigned from the Firm prior to sanctions being imposed by the Firm.

SANCTIONS

B. Respondent also consents to the imposition of the following sanctions:

1. A censure;
2. A fine in the amount of \$100,000.

The sanctions imposed herein shall be effective on a date set by FINRA staff.

Respondent agrees to pay the monetary sanction(s) upon notice that this AWC has been accepted and that such payment(s) are due and payable. Respondent has submitted an Election of Payment form showing the method by which it proposes to pay the fine imposed.

Respondent specifically and voluntarily waives any right to claim that it is unable to pay, now or at any time hereafter, the monetary sanction imposed in this matter.

II.

WAIVER OF PROCEDURAL RIGHTS

Respondent specifically and voluntarily waives the following rights granted under FINRA's Code of Procedure:

- A. To have a Formal Complaint issued specifying the allegations against the Firm;
- B. To be notified of the Formal Complaint and have the opportunity to answer the allegations in writing;
- C. To defend against the allegations in a disciplinary hearing before a hearing panel, to have a written record of the hearing made and to have a written decision issued; and
- D. To appeal any such decision to the National Adjudicatory Council ("NAC") and then to the U.S. Securities and Exchange Commission and a U.S. Court of Appeals.

Further, Respondent specifically and voluntarily waives any right to claim bias or prejudgment of the General Counsel, the NAC, or any member of the NAC, in connection with such person's or body's participation in discussions regarding the terms and conditions of this AWC, or other consideration of this AWC, including acceptance or rejection of this AWC.

Respondent further specifically and voluntarily waives any right to claim that a person violated the ex parte prohibitions of FINRA Rule 9143 or the separation of functions prohibitions of FINRA Rule 9144, in connection with such person's or body's participation in discussions regarding the terms and conditions of this AWC, or other consideration of this AWC, including its acceptance or rejection.

III.

OTHER MATTERS

Respondent understands that:

- A. Submission of this AWC is voluntary and will not resolve this matter unless and until it has been reviewed and accepted by the NAC, a Review Subcommittee of the NAC, or the Office of Disciplinary Affairs ("ODA"), pursuant to FINRA Rule 9216;
- B. If this AWC is not accepted, its submission will not be used as evidence to

prove any of the allegations against the Firm; and

C. If accepted:

1. this AWC will become part of Respondent's permanent disciplinary record and may be considered in any future actions brought by FINRA or any other regulator against the Firm;
2. this AWC will be made available through FINRA's public disclosure program in response to public inquiries about the Firm's disciplinary record;
3. FINRA may make a public announcement concerning this agreement and the subject matter thereof in accordance with FINRA Rule 8310 and IM-8310-3; and
4. The Firm may not take any action or make or permit to be made any public statement, including in regulatory filings or otherwise, denying, directly or indirectly, any finding in this AWC or create the impression that the AWC is without factual basis. The Firm may not take any position in any proceeding brought by or on behalf of FINRA, or to which FINRA is a party, that is inconsistent with any part of this AWC. Nothing in this provision affects Respondent's right to take legal or factual positions in litigation or other legal proceedings in which FINRA is not a party.

D. Respondent may attach a Corrective Action Statement to this AWC that is a statement of demonstrable corrective steps taken to prevent future misconduct. Respondent understands that it may not deny the charges or make any statement that is inconsistent with the AWC in this Statement. This Statement does not constitute factual or legal findings by FINRA, nor does it reflect the views of FINRA or its staff.

The undersigned, on behalf of the Firm, certifies that a person duly authorized to act on its behalf has read and understands all of the provisions of this AWC and has been given a full opportunity to ask questions about it; that it has agreed to its provisions voluntarily; and that no offer, threat, inducement, or promise of any kind, other than the terms set forth herein and the prospect of avoiding the issuance of a Complaint, has been made to induce Respondent to submit it.

6/8/09
Date

UBS Financial Services, Inc.

By:

Joy A. Weber
Joy A. Weber
Executive Director, Deputy General Counsel

Accepted by FINRA:

6/26/07
Date

Signed on behalf of the
Director of ODA, by delegated authority

Penny Rosenberg
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