

**FINANCIAL INDUSTRY REGULATORY AUTHORITY
LETTER OF ACCEPTANCE, WAIVER AND CONSENT
NO. 20100220936**

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

RE: UBS Securities LLC, Respondent
CRD No. 7654

Pursuant to FINRA Rule 9216 of FINRA's Code of Procedure, UBS Securities LLC ("UBS" or the "Firm") 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 Respondent 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 is an indirect and wholly owned subsidiary of UBS AG with its principal place of business in Stamford, CT. The Firm is a registered broker-dealer and futures commission merchant and provides a full range of investment banking services. The Firm is registered with the Securities & Exchange Commission and has been a member of the FINRA since August 1978.

RELEVANT DISCIPLINARY HISTORY

The Firm's relevant disciplinary history is as follows:

- UBS consented to findings that it failed to provide for appropriate procedures for supervision and control, including a separate system for follow-up and review reasonably designed to achieve compliance with NYSE Rules with respect to, among other things, retention of certain records pertaining to order information and order tickets. The Firm consented to a sanction consisting of a censure and a \$350,000 fine. See *UBS Securities LLC*, Decision No. 10-07 (NYSE Hearing Board March 15, 2010).

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- UBS consented to findings that its supervisory system did not include written supervisory procedures relative to its advertised trade volume in three securities to three service providers. The Firm consented to a sanction consisting of a censure and a \$200,000 fine. The Firm implemented written supervisory procedures prior to the resolution of this matter. See *UBS Securities, LLC*, AWC, FINRA Case No. 20060059871-01, December 2007.
- UBS consented to findings that it failed to provide for, establish, and maintain appropriate procedures of supervision and control, including a system of follow-up and review, with respect to operational and technological activities relating to delivery of product descriptions and prospectuses. The Firm consented to a sanction consisting of a censure and an \$800,000 fine. See *UBS Securities LLC*, Decision No. 07-114 (NYSE Hearing Board September 7, 2007).

OVERVIEW

Between January and May 2006 (the "Relevant Period"), UBS failed to reasonably supervise Francesco Fiske Rusciano ("Rusciano"), a junior trader on its Fixed Income Emerging Markets Latin American Desk (the "LatAm Desk") who, by various means, made false and inaccurate entries into the Firm's trading systems for non-deliverable forward ("NDF") transactions and Brazil 40 Bond transactions, which caused incorrect calculations of his risk positions and P&L, overstating his profits and understating his losses. In contrast to other traders on the LatAm Desk, the Firm gave Rusciano authority to enter NDF transactions directly into two trading systems. By manipulating these two trading systems, Rusciano was able to make undetected amended, late, mispriced and fictitious NDF transactions by which he concealed more than \$28 million dollars in trading losses. The Firm also failed to provide Rusciano's supervisor with reports concerning Rusciano's trading in NDFs and Brazil 40 bonds that were necessary to supervise Rusciano's activities.

Additionally, the Firm failed to have adequate written supervisory procedures for supervision of Rusciano's NDF trading and for the maintenance of books and records recording such NDF trading; and failed to make and keep current memoranda of the NDF transactions Rusciano entered for the Firm's account, improperly relying on its parent company, UBS AG, to keep these records on its behalf.

The foregoing violations resulted in the Firm's creation and maintenance of ledgers that inaccurately reflected unrealized profits and losses; and the risks associated with the NDF and Brazil 40 Bond positions.

FACTS AND VIOLATIVE CONDUCT

The Firm's LatAm Desk conducts trades of, among other things, Latin American corporate and sovereign bonds, derivatives and foreign exchange products including, NDFs. From January 2006 until June 2006 Rusciano was a junior trader on the LatAm Desk. While most traders on the LatAm Desk who traded NDFs did so as a hedging mechanism, Rusciano was permitted to trade NDFs as a primary product. Rusciano traded NDFs on a proprietary basis for the Firm. The non-deliverable forward contracts at issue in this case generally had a 30 to 60 day term and involved trades of the Brazilian Real for U.S. dollars or the reverse. On numerous occasions

from April through June 2006, Rusciano concealed from the Firm, by various means, more than \$28 million in trading losses he incurred in connection with his trades of Brazilian Real/U.S. Dollar NDF and Brazil 40 Bonds¹.

Non-Deliverable Forward Contracts

A non-deliverable forward contract is a short-term, cash-settled currency forward between two counterparties in the over-the-counter market. Non-deliverable forward contract holders are obligated to buy or sell the designated currency at specified prices and quantities on a specified future date. On the contracted settlement date, the profit or loss is determined based on the difference between the contracted non-deliverable forward rate and the fixing rate for that settlement date on an agreed amount. Non-deliverable forward contracts are commonly quoted for time periods of one month to one year, and are almost always settled in U.S. dollars.

The Relevant Trading Systems for Non-Deliverable Forward Contracts

During the Relevant Period, the LatAm Desk recorded its foreign exchange non-deliverable forward contracts for counterparty settlement purposes, and recorded its positions and the associated risk and profit and loss ("P&L") incurred from those positions through two separate systems – MOR and Indigo. Typically, LatAm Desk traders who traded NDFs did so as a hedging instrument and traded NDFs with FX traders on an internal desk. These LatAm Desk traders made their own NDF entry in Indigo but relied on the FX traders on an internal desk to make the MOR NDF entry on their behalf. The Firm permitted Rusciano to enter his NDF trades directly into both the MOR and Indigo systems. Rusciano was the only LatAm Desk trader who made his own NDF entries in both MOR and Indigo. Consequently, Rusciano was required to separately enter each NDF transaction into both systems. Though one of the Indigo entries generated an automatic corresponding entry in MOR, the two systems were not otherwise linked.

MOR

The MOR system belonged to and was maintained on the servers of UBS AG in Zurich, Switzerland.² All NDF contracts required entry into MOR. Rusciano made entries into MOR in order for his trades with street side counterparties to be confirmed and settled. UBS AG, not the Firm, confirmed and settled NDF trades with street-side counterparties. The Firm relied on UBS AG to confirm and settle NDF trades for the Firm's account. Information entered in MOR was received and maintained by UBS AG and not by the Firm.

¹ On or about February 9, 2010, Rusciano was barred from the securities industry pursuant to a decision issued by the NYSE Hearing Board based on his conduct in connection with this matter. See *In the Matter of Francesco Fiske Rusciano*, Decision No. 10-03 (NYSE Hearing Board February 9, 2010). Based on his conduct in this matter, Rusciano was also barred by the Board of Governors of the Federal Reserve from participating in the banking industry. See *In the Matter of Francesco Rusciano*, Docket Nos. 2009-007-1-E, 2009-007-1-CMP (Board of Governors of the Federal Reserve System November 25, 2009).

² As noted above, the Firm is a wholly owned subsidiary of UBS AG, which is not a FINRA-regulated broker dealer.

Indigo

The Indigo system also belonged to and was maintained on the servers of UBS AG. The LatAm Desk used the Indigo risk management system to record its risk positions and P&L. Indigo tracked the risk positions and P&L of each trader as well as the cumulative risk positions and P&L of the LatAm Desk. Rusciano was required to enter into Indigo full trade details of his NDF trades, including the counterparty, size of his transactions and contract price so that his P&L and risk reports would accurately reflect his positions and associated profits, losses and risk. Information entered in Indigo was received and maintained by UBS AG and not by the Firm.

Manipulation of the Trading Systems for NDF Transactions

In order to manipulate his P&L and risk exposure, Rusciano made fictitious entries into Indigo, delayed the entry of actual transaction data into Indigo, and amended both fictitious and actual trade data in Indigo on numerous occasions during the Relevant Period. For example, Rusciano was able to enter into NDF trades with the street and make entries into MOR so that trades could be confirmed and settled, and yet by not making corresponding entries into Indigo, prevent the position and profit or loss associated with those trades from being reflected on his P&L and risk reports. In addition, Rusciano delayed the entry of actual transaction data into MOR for unprofitable transactions, thereby causing repeated trade breaks in transactions with street-side counterparties. In each instance, Rusciano's presumed goal was to conceal an unrealized loss associated with an actual transaction and/or to create the appearance of a fictitious profit in connection with both actual and fictitious transactions.

Rusciano concealed losses of approximately \$28 million to the Firm through the conduct described above.

Supervision of Rusciano's NDF Transactions

The LatAm Desk was supervised by an appointed Desk Head who was responsible for its risk management and regulatory supervisory functions. During the Relevant Period, the Desk Head received supervisory reports on a daily basis. However, the Firm's electronic supervisory system did not capture NDF trade data and the reports forwarded to the Desk Head related only to P&L and risk information and did not contain records of Rusciano's daily trading activity. The Desk Head was not advised by the Firm that NDF trade data was not contained in the reports he received.

UBS AG personnel in Zurich created daily NDF-related reports including statements of profits and losses, risk positions, trade breaks, amended transactions, and reconciliations between MOR and Indigo, however the majority of these reports were not provided to the Desk Head and/or the Firm. For example, personnel in Zurich created an FX Hedge Reconciliation Report that identified any FX trades that were not entered into both MOR and Indigo. During the Relevant Period, the Desk Head was never provided with this report for supervisory review. Had the Firm been provided with the FX Hedge Reconciliation Reports for the Relevant Period, they would have readily disclosed numerous Rusciano NDF trades which had been entered in MOR but not Indigo or the reverse. Additionally, the Firm did not provide the Desk Head with any type of

trade break reports, amended transaction reports, or unmatched confirmation reports related to NDF transactions.

In other instances, relevant reports were provided to the traders but not to their supervisors. For example, UBS AG generated an unmatched confirmations report called "CCT Desk T+1" which reflected unmatched trade confirmations for NDF transactions. While this report was forwarded to Rusciano, it was not forwarded to Rusciano's supervisors for review.

Procedure for Amending NDF Transactions

Traders were permitted by the system to adjust, cancel and correct or otherwise amend their own NDF transactions in MOR provided the amendment or cancellation was made on trade date. After trade date, traders were not permitted by the system to amend or cancel a trade in MOR. Instead, personnel of UBS AG could and did amend or cancel NDF transactions in MOR after trade date based on instructions from the Firm's traders. The Firm did not require supervisory approval to execute traders' instructions to amend or cancel NDF trades in MOR and did not assess the legitimacy of the amendment and/or cancellation. This process was not a control process.

Procedure for Confirmation of NDF Transactions

NDF transactions entered by traders of the LatAm Desk in Stamford, CT were confirmed and settled in Zurich. Copies of Rusciano's NDF confirmations and related documents were not forwarded to the Firm.

Books and Records of NDF Trades

NDF transactions for the Firm's account were entered into the MOR and Indigo systems which belonged to and were maintained by UBS AG. The NDF records received and maintained by UBS AG for the Firm's account included a memorandum of each purchase and sale for the account of the Firm showing, among other things, the price, time of receipt and terms and conditions of the order.

When Rusciano entered an NDF trade into MOR and/or Indigo, the data was received, and the P&L was computed and reviewed by UBS AG. The P&L data was uploaded by UBS AG on a daily basis into a database accessible by UBS Securities personnel. Once the P&L data was uploaded, staff of UBS AG notified Firm personnel that the data was available. Firm personnel then extracted the data and consolidated it with other P&L for the LatAm Desk and its traders. Rusciano's inaccurate, late and omitted entries into the MOR and Indigo systems caused the P&L and risk position data on UBS Securities' books to be inaccurate.

Brazil 40 Bond Transactions

Brazil 40 Bond¹ trades were executed by the LatAm Desk with the counterparty and subsequently entered into the Bloomberg Trading System. The Bloomberg Trading System was

¹ In August 2000, Brazil issued \$5.16 billion in new 40-year global bonds in exchange for \$5.22 billion in old Brady Bonds. The Brazil 40 Bonds, denominated in U.S. dollars, is due in 2040.

used by the Firm to record transactions for settlement, position recording and P&L purposes. The Brazil 40 Bond trades settled on a T+3 basis. Traders were required to enter all the details of their bond transactions into the Bloomberg Trading System and each trader had a unique password by which they gained access to that system.

Rusciano entered data regarding his Brazil 40 Bond trades as required and initially accurately. However, on one or both of the two days between trade date and settlement date, Rusciano manipulated the price of the transactions in Bloomberg in order to conceal losses and/or create the appearance of a fictitious and/or inflated profit on the trades. On settlement date, Rusciano finally adjusted the prices in Bloomberg back to the actual transaction prices in order to avoid trade breaks.

Rusciano concealed losses to the Firm of approximately \$700,000 through various false entries made in the Firm's Bloomberg system.

Supervision of Rusciano's Brazil 40 Bond Transactions

Rusciano's Brazil 40 Bond data was not captured by the Firm's electronic supervisory system. Although the Firm generated reports for use in the supervision of bond transactions, these reports did not capture Rusciano's bond trading data. Thus, Rusciano's trading of Brazil 40 Bonds was not captured within the Firm's supervisory exception reports and therefore, not supervised.

The Firm's Policies and Procedures

The Firm's Fixed Income, Rates and Currencies Supervisory Procedures Manual (the "Fixed Income Manual"), in effect during the Relevant Period, required Desk Heads to "continually assess and monitor the activities taking place on their respective desks and be alert for signs of conduct that are unusual, questionable, or suspicious."

The Firm's Supervisory Procedures Manual: Investment Grade Corporates Emerging Markets Trading (the "Emerging Markets Manual"), directed Desk Heads to focus their attention on a variety of areas, including order entry, adjusted trading and amended transactions. According to the Emerging Markets Manual, Desk Heads were provided a variety of reports to assist in the execution of their supervisory duties, including Daily Activity Reports, Profit and Loss Reports and Unallocated/Fails Reports.

Supervisory Violations

NASD Rule 3010 requires members to, among other things, "establish and maintain a system to supervise the activities of each registered representative, registered principal, and other associated person that is reasonably designed to achieve compliance with applicable securities laws and regulations, and with applicable NASD Rules. Final responsibility for supervision shall rest with the member." The rule further provides that "[e]ach member shall establish, maintain, and enforce written procedures to supervise the types of business in which it engages and to supervise the activities of the registered representatives, registered principals, and other associated persons that are reasonably designed to achieve compliance with applicable securities laws and regulations, and with the applicable rules of NASD."

NASD Rule 2110 provides that "[a] member in the conduct of its business, shall observe high standards of commercial honor and just and equitable principles of trade." Violations of federal securities laws and NASD Rules, are viewed as violations of Rule 2110 because members of the securities industry are expected and required to abide by the applicable rules and regulations.

Rusciano was the only trader on the LatAm Desk who was given authority to enter his NDF transactions into both the MOR and Indigo systems. This use of two internal trading systems for the entry of NDF transactions required appropriate supervision. The Firm's existing policies and procedures did not adequately address Rusciano's ability to make entries directly into both MOR and Indigo. The Firm's electronic supervisory system did not capture NDF trade data and the Firm failed to establish supervisory systems or procedures to reasonably ensure that Rusciano's entries were complete and accurate and that his MOR and Indigo entries matched. The Firm likewise failed to establish policies and procedures providing for its creation and maintenance of required books and records of NDF transactions entered for its account.

Additionally, the Firm failed to have written supervisory procedures, for the amending, settling and confirming of NDF transactions. Amendments to NDF transactions were completed either by the trader himself or by support staff in Zurich at the direction of the trader without any supervisory controls or the requirement for supervisory approval. Likewise, the process for confirmation and settlement of NDF transactions was completed in Zurich by staff of UBS AG, who forwarded questions and problems not to the traders' supervisor but rather to the trader himself. Supervisory notifications were only made in those cases in which the matter could not be otherwise resolved. This process permitted Rusciano's activities to go undetected by the Firm.

The Firm further failed to provide the Desk Head with reports regarding amended, mismatched and/or missing NDF trades by Rusciano as well as reports of trade breaks relating to Rusciano's NDF trading. Likewise, because Rusciano's bond book was excluded from the Firm's electronic supervisory system, the Firm failed to provide the Desk Head with data concerning Rusciano's Bond trades which would have disclosed his manipulation of the Brazil 40 Bond trades. To the extent that P&L and risk position data was available for supervisory review, the data was inaccurate based on Rusciano's false, delayed and fictitious entries. In sum, the Firm failed to provide the Desk Head with the information or systems necessary to reasonably supervise Rusciano's trading activity because, it failed to provide him with records of Rusciano's NDF and Brazil 40 Bond transactions, relevant MOR and Indigo entries, and accurate P&L and risk position reports for the NDF and Brazil 40 Bond trades.

As a result of the foregoing conduct, the Firm violated NASD Rule 3010 and 2110 by failing to (a) adequately monitor the trading activities of a proprietary trader on its LatAm Desk to detect and prevent the trader from making late and inaccurate entries into various Firm trading systems, thereby concealing his actual positions and associated losses in proprietary accounts he managed for UBS; (b) provide qualified supervisors with the information necessary to supervise a proprietary trader on its LatAm Desk; (c) establish and maintain adequate written procedures for the supervision of the trading of NDF contracts on its LatAm Desk; and (d) establish and maintain adequate written procedures for the creation and maintenance of certain required books and records for NDF trading on its LatAm Desk.

Books and Records Violations

Section 17(a) of the Securities Exchange Act of 1934 (the "Act") and Rule 17a-3 thereunder require every broker or dealer registered pursuant to Section 15 of the Securities Exchange Act of 1934 to make and keep current certain books and records related to its business. These include (1) a memorandum of each purchase and sale for the account of the member, broker, or dealer (Rule 17a-3(a)(7)) and (2) ledgers (or other records) reflecting all assets and liabilities, income and expense and capital accounts (Rule 17a-3(a)(2)). Unlike other subdivisions of Rule 17a-3, the referenced subdivisions do not limit the requirement to records of transactions involving securities¹. NASD Rule 3110 requires each member to preserve books and records in conformity with Section 17a of the Act.

The Firm failed to make and keep current a memorandum of each NDF transaction entered by Rusciano, as required by Rule 17a-3(a)(7). As described above, Rusciano traded NDFs on a proprietary basis for the Firm through the MOR and Indigo systems which belonged to and were maintained on the servers of UBS AG. Thus, the NDF records, which included a memorandum of each purchase and sale for the Firm's account, were created and maintained by UBS AG, not the Firm.

Additionally, based on the false, delayed and fictitious entries made by Rusciano in connection to his NDF and Brazil 40 Bond transactions, the Firm's records of his and the LatAm Desk's overall P&L and corresponding risk positions were not accurate, as required by Rule 17a-3(a)(2).

As a result of the foregoing conduct, the Firm violated Section 17(a) of the Securities Exchange Act of 1934 and Rules 17a-3(a)(2), 17a-3(a)(7) and 17a-4(i) thereunder and NASD Rule 3110(a) and 2110 by failing to: (a) make and keep a memorandum of certain NDF transactions entered for the Firm's account; (b) make and keep current ledgers accurately reflecting its assets and liabilities in that it failed to accurately account for unrealized profits and/or losses associated with its Brazil 40 Bond and certain NDF positions; and (c) make and keep current ledgers accurately reflecting the risks associated with its Brazil 40 bond and certain NDF positions.

When the issues concerning Rusciano's trading came to light, the Firm conducted an internal investigation to identify the errant bond and NDF transactions and calculate the losses incurred in connection with them. Thereafter, the Firm instituted remedial measures to prevent a recurrence in the future.

B. The Firm also consents to the imposition of the following sanctions:

- a. A censure; and
- b. A fine in the amount of \$600,000.

The Firm agrees to pay the monetary sanction upon notice that this AWC has been accepted and that such payment is due and payable. The Firm

¹ A NDF is a forward contract, not a security. However, the NDFs at issue involve foreign currency and are specifically exempt from regulation as a futures contract. See *Treasury Amendment to the CEA*, 7 U.S.C.S. §2.

has submitted an Election of Payment form showing the method by which it proposes to pay the fine imposed.

The Firm 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.

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

II.

WAIVER OF PROCEDURAL RIGHTS

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

- A. To have a Complaint issued specifying the allegations against it;
- B. To be notified of the 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, the Firm 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.

The Firm 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

The Firm 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 me; and
- C. If accepted:
 - 1. this AWC will become part of the Firm's permanent disciplinary record and may be considered in any future actions brought by FINRA or any other regulator against it;
 - 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 8313; 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 the Firm's right to take legal or factual positions in litigation or other legal proceedings in which FINRA is not a party.
- D. The Firm may attach a Corrective Action Statement to this AWC that is a statement of demonstrable corrective steps taken to prevent future misconduct. The Firm 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 the Firm 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 the Firm to submit it.

09/10/2010
Date (mm/dd/yyyy)

Abby Meiselman
UBS Securities LLC

By: Abby Meiselman

09/09/2010
Date (mm/dd/yyyy)

Andrew Dragomiris
UBS Securities LLC

By: ANDREW DRAGOMIRIS

Reviewed by:

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Accepted by FINRA:

September 29, 2010
Date

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

Susan Light
Susan Light
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