

STATE OF ALASKA
DEPARTMENT OF COMMUNITY AND ECONOMIC DEVELOPMENT
DIVISION OF BANKING, SECURITIES, AND CORPORATIONS
P.O. BOX 110807
JUNEAU, ALASKA 99811-0807

IN THE MATTER OF:)

UBS Warburg, LLC)
677 Washington Boulevard)
Stamford, Connecticut 06901)
CRD # 7654)

Alaska Order 04-07 S

CONSENT ORDER

UBS PaineWebber Inc.)
1285 Avenue of the Americas)
New York, New York 10019)
CRD # 8174)

Respondents.)

WHEREAS, UBS PaineWebber Inc. ("UBS PaineWebber") is a broker-dealer registered in the State of Alaska since 1970; and

WHEREAS, UBS Warburg LLC ("UBS Warburg") is a broker-dealer registered in the State of Alaska since 1991; and

WHEREAS, for purposes of this Order, PaineWebber, UBS PaineWebber and UBS Warburg will be collectively referred to as UBS or the Firm, except in circumstances where PaineWebber, UBS PaineWebber or UBS Warburg are specifically referenced; and

WHEREAS, coordinated investigations into the Firm's activities in connection with certain of its equity research practices during the period of approximately 1999 through 2001 have been conducted by a multi-state task force and a joint task force of the U.S. Securities and Exchange Commission ("SEC"), the New York Stock Exchange ("Exchange"), and the National Association of Securities Dealers ("NASD") (collectively, the "regulators"); and

WHEREAS, the Firm has advised regulators of its agreement to resolve the issues raised in the investigations relating to its research practices; and

WHEREAS, the Firm agrees to implement certain changes with respect to its research practices to achieve compliance with all regulations and any undertakings set forth or incorporated herein governing research analysts, and to make certain payments; and

WHEREAS, the Firm elects to permanently waive any right to a hearing and appeal under AS 45.55.940 with respect to this Administrative Consent Order (the "Order");

1 NOW, THEREFORE, the Alaska division of banking, securities, and corporations
(division), as administrator of the Alaska Securities Act (Act), hereby enters this Order:

2 I.

3 The Firm admits the jurisdiction of the Alaska division, neither admits nor denies the
Findings of Fact and Conclusions of Law contained in this Order, and consents to the entry of
4 this Order by the division.

5 **FINDINGS OF FACT**

6 **1. Background and Jurisdiction**

- 7 1) UBS Warburg became a member organization of the Exchange on September 6, 1985. It is
8 principally owned by UBS AG (UBS AG was formed through the June 1998 merger of Union
9 Bank of Switzerland with Swiss Bank Corporation) and is engaged in the business of global
10 investment banking and securities. UBS Warburg also provides services on a worldwide
11 basis, including investment banking, securities trading and principal investments, and asset
12 management. The principal office of UBS Warburg is located at 677 Washington Boulevard,
13 in Stamford, Connecticut.
- 14 2) PaineWebber Inc. ("PaineWebber"), founded in 1879, was a full-service securities firm
15 located in New York, and became a member of the Exchange on November 17, 1982. The
16 services provided by PaineWebber, on a global basis, included investment banking,
17 research, trading, investing on a principal basis, and asset management.
- 18 3) On November 3, 2000, UBS AG purchased PaineWebber and PaineWebber became known
19 as UBS PaineWebber. UBS PaineWebber is indirectly owned by UBS AG. As part of the
20 merger, PaineWebber banking and research activities were shifted to UBS Warburg LLC,
21 and some investment bankers and research analysts previously employed by PaineWebber
22 became employees of UBS Warburg LLC. Since the merger, UBS PaineWebber is
23 principally engaged in the business of servicing retail investors and no longer employs
24 equity investment bankers or research analysts. UBS PaineWebber's principal office is
25 located at 1285 Avenue of the Americas, New York, New York.
- 4) UBS AG has offices in over 50 countries, employing approximately 69,500 people, 35,000 of
whom work for UBS PaineWebber or UBS Warburg. UBS Warburg has 90 stock exchange
memberships in 30 countries and the firm's 500 equity research analysts cover about 3,300
companies world-wide.
- 5) UBS Warburg and UBS PaineWebber are registered with the Exchange, SEC, NASD and
with all 50 states, the District of Columbia and Puerto Rico.

6 **B. Overview**

- 7 6) This action concerns the research and investment banking activities at UBS Warburg during
8 the period July 1, 1999 through June 30, 2001 as well as the research and investment
9 banking activities at PaineWebber from July 1, 1999 until its merger with UBS AG on
10 November 3, 2000 (the "relevant periods").
- 11 7) During the relevant period, as set forth below, the Firm sought and did investment banking
12 business with many companies covered by the Firm's Research Department. Research
13 analysts were encouraged to participate in investment banking activities and that was a
14 factor considered in the analysts' compensation. In addition, the decision to initiate and
15 maintain research coverage of certain companies was in some cases coordinated with the
16 Investment Banking Department and influenced by investment banking interests.

- 1 8) As a result of the foregoing, as set forth below, certain research analysts at the Firm were
2 subject to investment banking influences and conflicts of interest between supporting the
investment banking business at the Firm and publishing objective research.
- 3 9) As set forth below, the Firm had knowledge of these investment banking influences and
4 conflicts of interest, yet failed to establish and maintain adequate policies, systems and
procedures with respect to research analysts that were reasonably designed to detect and
prevent those influences or manage those conflicts.

5 **C. The Role of the Research Analyst**

- 6 10) Research analysts were responsible for providing analyses of the financial outlook of
7 particular companies in the context of the business sectors in which those companies
operate and the securities markets as a whole.
- 8 11) The Firm publishes research on publicly traded companies based upon analysts' examining,
9 among other things, financial information contained in public filings, questioning company
management, investigating customer and supplier relationships, evaluating companies'
10 business plans and the products or services offered, building financial models, and
analyzing competitive trends.
- 11 12) After synthesizing and analyzing this information, analysts produced research in the form of
12 full reports and more abbreviated formats that typically contained a rating, a price target,
and a summary and analysis of the factors that generated the rating and/or price target.
13 The Firm then distributed its analysts' research reports to the Firm's institutional clients, to
the Firm's sales force and to retail clients upon request. Research reports were also made
14 available to third party vendors, such as Bloomberg and First Call, who then made the
reports available to subscribers to those vendors. In addition, the rating, but not the analysis
15 contained in the research report, was published on Internet websites such as Multex, for
viewing by the investing public. Similarly, UBS Warburg posted on its website (and provided
16 in hard copy if requested), monthly summaries concerning the companies covered by its
research analysts, the ratings issued, and any ratings changes from the previous month.
17 These summaries did not include any of the analyses contained in the actual research
reports.
- 18 13) Analysts were required according to UBS Warburg policy to submit any proposed rating
upgrades or downgrades and initiations of coverage to an Investment Review Committee
19 ("IRC") that consisted of compliance, institutional sales, equity capital markets and research
department personnel. The IRC reviewed analysts' reports and approved rating and target
changes as well as initiations of coverage.
- 20 14) Nevertheless, analysts were sometimes able to upgrade or downgrade ratings by requesting
21 and receiving approval of one of several designated members of Research Management,
who were also members of the IRC, rather than the full IRC, whenever that change in rating
22 was based upon breaking news. Because Firm analysts sometimes changed their ratings
based upon breaking news, upgrades or downgrades were authorized without the approval
23 of the full IRC in nearly one-third of the instances in which ratings were changed during the
Relevant Period.
- 24 15) Analysts also made themselves available to the Firm's institutional and retail sales force to
25 answer questions about the sector and the covered companies. In addition, analysts
provided periodic research updates to the Firm's sales force through "morning calls" or
"morning notes," which are daily pre-market opening discussions of the market sectors and
specific covered companies. Analysts also provided research updates through "blast" e-

1 mails and voice messages, which typically provide a rating and a more abbreviated analysis
2 than what is contained in a research report.

3 16) During the Relevant Period, analysts were expected to make independent determinations
4 regarding coverage, stock price targets and ratings whether to buy, sell or hold certain
5 stocks, without consideration of their research reports' potential impact upon Firm
6 investment banking business or the business of Firm investment banking clients.

7 17) In the 1990's the importance of research issued by analysts increased as a result of the
8 dramatic growth in the number of individual investors and the availability of online trading.
9 Research coverage became a marketing tool, and issuers sometimes chose an investment
10 bank based upon the expectation that a certain analyst would cover the company's stock
11 favorably.

12 18) As the performance and coverage of research analysts became increasingly integral to the
13 awarding of investment banking business, the Firm encouraged its research analysts to
14 become more involved in investment banking activities, including marketing securities
15 issued by investment banking clients (primarily to the Firm's institutional clients) and
16 soliciting investment banking business.

17 **D. Research Analyst Participation in Investment Banking Activities**

18 19) The Investment Banking Division at the Firm advised corporate clients and helped them
19 execute various financial transactions, including the issuance of stock and other securities.
20 The Firm frequently served as one of the underwriters in initial public offerings ("IPOs") – the
21 first public issuance of stock of a company that has not previously been traded – and follow-
22 on offerings of securities.

23 20) During the relevant period, investment banking was an important source of revenues and
24 profits for UBS Warburg. UBS Warburg's investment banking department reported global
25 revenues of \$1.369 billion in 1999, \$1.602 billion in 2000 and \$1.369 billion in 2001,
representing nearly 15% of UBS Warburg's global revenues during that time period.

26 21) In addition to performing research functions, some of the Firm's research analysts identified
27 companies as prospects for investment banking services, participated in "pitches" of the
28 Firm's investment banking services to companies, and participated in "roadshows" and other
29 activities in connection with the marketing of underwriting transactions. At times, Firm
30 research analysts were involved in meetings between companies, prior to their IPO's, and
31 some of the Firm's institutional customers who had expressed an interest in purchasing
32 shares in those IPOs. These meetings would take place in various cities all over the country
33 in order to accommodate the institutional customers and were commonly known in the
34 industry as "analyst roadshows."

35 22) During these roadshows, the analyst would discuss the issuer with the institutional
customers and would frequently arrange "one on one" meetings between company
executives and managers of institutional clients who had expressed interest in investing.
These roadshows were considered to be a service provided by the Firm to both its
institutional clients as well as its investment banking clients.

24 23) Research analysts also participated in commitment committee and due diligence activities in
25 connection with underwriting activities and assisted the Investment Banking Department in
providing merger and acquisition and other advisory services to companies.

24) The interactions between investment bankers and certain research analysts during the

1 Relevant Period, at times impacted the independence of those analysts' as they became
2 increasingly involved in the Firm's efforts to secure investment banking business. As a
3 result, an environment was created that may have led certain analysts to believe that they
4 were expected to initiate and maintain positive research about Firm clients.

5 **E. Participation in Investment Banking Activities was a Factor in Evaluating and**
6 **Compensating Research Analysts**

7 25) The compensation system at the Firm provided an incentive for research analysts to
8 participate in investment activities and to assist in generating investment banking business
9 for the Firm.

10 26) The performance of research analysts was evaluated by Research Management through a
11 annual review process and analysts' bonuses were determined through this process, unless
12 an analyst had a guaranteed bonus set by contract in advance. The guaranteed bonuses
13 for the Firm's top analysts were frequently in the millions of dollars while the base salary was
14 typically in the \$125,000 to \$150,000 range.

15 27) In addition to these guaranteed bonuses, six PaineWebber analysts were explicitly
16 guaranteed "investment banking bonuses", meaning that those analysts were entitled to
17 some portion of certain investment banking fees earned by PaineWebber.

18 28) For example, two PaineWebber analysts were promised compensation equal to 15% of the
19 underwriting management fees earned in their respective sectors. In addition to the
20 bonuses paid to those analysts pursuant to PaineWebber's annual review process, those
21 two analysts received an additional \$125,000 and \$135,000, respectively, for the year 2000
22 because of the investment banking fees earned by PaineWebber in their respective sectors.

23 29) When UBS Warburg acquired the research and investment banking operations of
24 PaineWebber in November, 2000, the Firm removed the direct link between investment
25 banking revenues and analyst compensation.

30) The UBS annual evaluation process included an evaluation of each analyst's contribution
31 to the Firm's investment banking business as a factor in determining bonus compensation.

32) Each year, prior to bonuses being paid, UBS conducted a comprehensive evaluation
33 process that rated each analyst's performance and assigned analysts rankings in one of four
34 quartiles. As part of that process, analysts submitted self-evaluations, and other UBS
35 employees with whom the analyst had had significant contact were also asked to submit
36 evaluations, including investment bankers.

37 32) In describing the analysts' performance, the UBS bankers frequently included comments
38 relating to the analyst's abilities to attract and/or maintain investment banking clients.

39 33) For example, an investment banker at UBS Warburg evaluated one analyst as "the best
40 business builder in research I have ever known."

41 34) Similarly, Research Management considered investment banking contributions as a
42 component of analysts' performance evaluations. The Head of UBS Warburg's Research
43 Division evaluated that same analyst as the "most prolific analyst at the firm when it comes
44 to generating investment banking revenues" and that he "manages the tightest coordination
45 between research and [the Corporate Finance Division] of any sector." This evaluation was
46 included in the section of the performance review entitled "Accomplishment/Strengths."

1 35) Furthermore, the Head of UBS Warburg's Research Division, who was ultimately
2 responsible for evaluating analysts and determining the exact amount of their bonus
3 compensation, referenced analysts' contributions to investment banking business as one
4 factor in the evaluation of their performance.

5 36) The Firm also specifically requested that analysts, in writing their own self-evaluations,
6 include, among other criteria, an assessment of their contribution to the Firm's Investment
7 Banking Department. This led to a perception among analysts that contribution to
8 investment banking was a factor in compensation.

9 37) In response to this request, one analyst described his own performance for the Firm by
10 highlighting his involvement with several investment banking deals done by the Firm during
11 the previous year. The analyst then boasted that he was responsible for generating \$15
12 million in investment banking revenue for the Firm during that time.

13 **F. Investment Banking Interests Influenced the Firm's Decisions to Initiate**
14 **and Maintain Research Coverage**

15 38) In general, the Firm determined whether to initiate and maintain research coverage based
16 upon investor interest in a company or based upon investment banking considerations, such
17 as attracting companies to generate investment banking business or maintaining a positive
18 relationship with existing investment banking clients.

19 39) As a matter of practice, the Firm initiated coverage on companies that engaged the Firm in
20 an investment banking transaction and maintained coverage for a period of time beyond the
21 transaction.

22 40) Research analysts were aware that, in certain circumstances, their positive and continued
23 coverage of particular companies was an important factor for the generation of investment
24 banking business. Thus, some research analysts and investment bankers coordinated the
25 initiation and maintenance of research coverage based upon, among other things,
investment banking considerations.

41) For example, analysts were required to seek authorization from Research Management prior
to dropping coverage of a company, unless the reason for dropping coverage was due the
departure of the covering analyst. However, when the company involved was an investment
banking client, the analyst was also expected to consult with the investment banking
personnel responsible to that client.

42) Additionally, according to an e-mail by UBS Warburg Head of Global Technology Investment
Banking, it was an implicit condition in the UBS Warburg investment banking agreements
that UBS Warburg would continue to provide research coverage of its clients for a period of
time following a transaction. Such implied promises to investment banking clients impacted
the Research Department's authority to make its own independent determinations
concerning the continuation of coverage.

43) When a UBS Warburg analyst informed the Head of the Research Department that he
intended to drop coverage of a particular company, he was asked whether there was any
"banking relationship" and was told to "check with" the banker who worked with that
company.

44) Although coverage of the company was dropped in that instance, the lead banker of the
technology group at UBS Warburg reminded the research analyst and Research
Management of the implicit promise made during pitch meetings that coverage would be

1 maintained for a significant period of time: "The problem is that many companies . . . in
2 asking for credentials for a pitch will ask directly if we are meeting our research obligations
3 to the companies we bank. They generally expect an IPO fee to justify coverage for three
4 years . . ."

5 45) In another instance, when a UBS Warburg research analyst informed his banking
6 counterpart, that he intended to drop coverage of four biotechnology companies, the banker
7 forwarded that message to a member of Investment Banking Management who sent an e-
8 mail to the analyst stating that he wished "to have the opportunity to discuss future potential
9 revenue opportunities from these clients" before coverage was dropped.

10 46) The Investment Banking Department also sometimes had an impact upon determinations
11 made by analysts regarding the initiation of coverage. When investment bankers became
12 aware of opportunities to cultivate investment banking business, they sometimes suggested
13 to the analyst in that sector that coverage should be initiated.

14 47) For example, a Firm investment banker sent an e-mail to a Firm research analyst indicating
15 that a company with whom he had discussed investment banking business had asked "if
16 there was an interest by UBS Warburg to cover them from a research stand point." The
17 banker went on to say that he believed that "the timing is good" for initiation of research
18 coverage of the company and offered to set up a meeting between the company and the
19 analyst.

20 48) Similarly, a Firm analyst informed his banking counterparts that they should wait to call a
21 company to discuss a potential investment banking deal until "after I pick up coverage."

22 **G. The Firm's Pitch Materials Contained Discussions of Research Coverage**

23 49) During the relevant period, research coverage was an important factor considered by
24 companies in selecting a firm for an investment banking transaction.

25 50) Certain analysts understood that the issuance of positive research about an issuer was a
pre-condition to the Firm's obtaining the issuer's banking business.

51) In competing for investment banking business from prospective issuers, the Firm typically
sent investment bankers to meet with company management in order to persuade the
company to select the Firm as one of the underwriters in a contemplated transaction.
Research analysts often accompanied bankers on these "pitch" meetings. At these
meetings, Firm investment bankers would present their level of expertise in the company's
sector and discuss their previous experience with other companies, as well as their view of
the company's merits and likelihood of success.

52) In some instances, the research analyst's coverage and impact on the market place
concerning companies under coverage was a component of the pitch presented by the Firm.
As a result of these presentations, certain issuers selected an investment bank because of
the reputation of the analyst that would cover the company's stock and the issuer's belief
that the coverage would be positive.

53) Furthermore, certain research analysts who covered the company's sector often worked with
investment bankers to prepare the Firm's pitch presentation and attended the pitch meeting.

54) In preparation for each presentation, the investment bankers, sometimes with an analyst's
input, prepared a "pitch book" that was distributed at the meeting and contained a summary
of the Firm's presentation.

- 1 55) Some pitch books contained information relating to the company, its competition, the sector
2 in which it operated and the nature of the services the Firm could provide to the company
3 and its shareholders after the completion of a potential offering. Additionally, Firm pitch
4 books sometimes contained implicit representations that the Firm would continue to provide
5 service to the issuer after the offering by providing research coverage about the company.
- 6 56) Some pitch books contained information indicating that a specific analyst would cover the
7 company and included data demonstrating how that analyst's positive comments about
8 other companies in the sector had had a direct positive impact upon the stock prices of
9 those companies.
- 10 57) For example, the pitch book presented to JDS Uniphase by PaineWebber, discussed the
11 impact that PaineWebber research had on covered stocks by including a graphic depicting
12 the performance of stocks on the Firm's "Buy List" as opposed to stocks on the Firm's
13 "Attractive List" and "Neutral List." At the top of the graphic, PaineWebber quoted a report
14 from Reuters which stated, "Shares of semiconductor companies specializing in chips for the
15 communications market rose on Thursday after PaineWebber published a report citing the
16 sector's growth prospects."
- 17 58) Similarly, in a pitch book presented to Avant Immunotherapeutics, Inc., PaineWebber
18 presented a slide entitled "Demonstrated Strength in Equity Trading and Research." One of
19 the sub-topics on the slide stated, "Buy and attractive recommendations have outperformed
20 the S&P 500 by 84 percentage points for the period 1/90 through 12/99" while "Sell and
21 unattractive ratings have underperformed the S&P 500 by 361 percentage points for the
22 period 1/90 through 12/99."
- 23 59) Because analysts often participated in the Firm's efforts to win investment banking business,
24 analysts were sometimes subjected to competing pressures after a stock became publicly
25 traded. The type of information contained in the pitch books, such as the examples above,
implied to issuers that the Firm would provide positive research coverage if selected for an
investment banking transaction, and that such coverage could result in rising stock prices for
those companies.

H. Research Analysts Rarely Issued Neutral or Negative Ratings

- 18 60) During the relevant period, PaineWebber's rating system allowed research analysts to
19 assign one of four ratings to a stock: "Buy", defined as total return expected to exceed that
20 of the S&P 500 by 20 percentage points or more over the next 12 months; "Attractive", 12
21 month total return potential that is 10-20 percentage points greater than the market's;
22 "Neutral", 12 month total return potential within 10 percentage points of the market's;
23 "Unattractive", expected to underperform the market by more than 10 percentage points on
24 a total return basis over the next 12 months.
- 25 61) During the relevant period, UBS Warburg's rating system differed slightly from
PaineWebber's and allowed research analysts to assign one of five ratings to a stock:
"Strong Buy", defined as greater than 20% excess return potential; "Buy", positive excess
return potential; "Hold", low excess return potential; "Reduce", negative excess return
potential; "Sell", greater than 20% negative excess return potential. All of these ratings
related to a 12 month time horizon.
- 62) During the relevant period, the level of the price target and the strength of the
recommendation placed on a stock by covering analysts sometimes had a significant impact
on the stock price. Investment bankers and issuers, being fully aware of the potential

1 impact of analysts' recommendations, were motivated to seek research coverage containing
2 positive recommendations.

3 63) In fact, certain analysts considered the investment banking implications for the Firm when
4 contemplating issuing even a neutral rating about an investment banking client. For
5 example, a member of Equity Sales Management, sent an e-mail to one of UBS Warburg's
6 telecom analysts stating "The salesforce is extremely frustrated with your research, price
7 targets, ratings . . . They feel that you're being somewhat flippant and not taking
8 responsibility for your recommendations and for having lost hundreds of millions of dollars
9 for people." The analyst responded that he would never utilize a Hold rating on a stock
10 unless one of two conditions occurred: "1) if I believe the company is about to go bankrupt;
11 2) if there is no investment banking business to be had there."

12 64) Notwithstanding that PaineWebber had four available ratings and UBS Warburg had five,
13 the Firm's research analysts rarely issued ratings other than "Strong Buy" and "Buy" on the
14 stocks of investment banking clients. Out of several thousand companies covered by UBS
15 Warburg during the relevant period, UBS Warburg issued only seven "Hold" ratings and two
16 "Sell" ratings on companies with which it had an investment banking relationship.

17 65) Similarly, from July 1, 1999 until the time of the merger, PaineWebber issued only sixteen
18 "Neutral" ratings and five "Unattractive" ratings on companies with which it had an
19 investment banking relationship.

20 **I. In Certain Instances, the Firm Published Exaggerated or Unwarranted Research**

21 66) On several occasions, the conflicts of interest discussed above resulted in analysts
22 publishing ratings and/or recommendations that were exaggerated or unwarranted, and/or
23 contained opinions for which there was no reasonable basis. The following are examples of
24 how these conflicts affected the research:

25 67) In April of 1998, UBS Warburg served as the lead manager on an IPO for Triangle
Pharmaceuticals ("Triangle") and received \$1.8 million in investment banking fees.

68) Notwithstanding a market capitalization value of approximately \$352,000,000, in November
of 1999, Triangle had yet to earn any revenue. Rather, investor optimism for the stock was
based upon the anticipated approval by the Food and Drug Administration ("FDA") of
several new drugs, including its "lead HIV drug", Coactinon.

69) In a research report issued on October 8, 1999, the UBS Warburg research analyst who
covered Triangle issued a research report that maintained a "Buy" rating while relaying news
to investors that a study of the drug Coactinon had proved "inconclusive." The analyst also
wrote that the form of testing used by Triangle to gain approval from the FDA had been used
before but "had been in less favor recently," and that accordingly it "is unclear what the
FDA's requirements will now be" for testing the drug.

70) On December 10, 1999, the FDA informed the company that it would require an additional
round of testing, which would cause at least a substantial delay, and perhaps ultimately a
cancellation, of the release and sale of the drug. As a result the stock price fell more than
\$3 -- or 23% -- from \$15.63 to \$12.00 on the date of the announcement.

71) On that same day, the analyst published a new research report in which she relayed the
news to investors but maintained her "Buy" rating, based in part, according to the report,
upon the analyst's belief that a different drug in development by Triangle was the company's
"most important near-term opportunity."

- 1 72) The analyst spoke to the UBS Warburg sales force before the market opened following
2 Triangle's announcement of the FDA's decision and made a statement in form or in
3 substance that the FDA's action had been an anticipated possibility notwithstanding the
4 analyst's "Buy" rating on the stock.
- 5 73) Following that call, a member of UBS Warburg's Equity Trading Management contacted the
6 analyst by e-mail and expressed disappointment that the analyst anticipated that the FDA
7 might take this action but had failed to adequately emphasize that possibility to the sales
8 force.
- 9 74) The analyst responded that her failure to emphasize negative information regarding Triangle
10 was, at least partially, a result of the analyst's allegiance to the investment banking client:
11 "Triangle is a very important client of [the firm]. We could not go out with a big research call
12 trashing their lead product, although we had a feeling the FDA might balk. Had we been
13 right or wrong, it would have been a disaster. I just wanted the salesforce to know we were
14 not surprised, and that where appropriate we had had some conversations with the buy-side.
15 Sorry this was not conveyed."
- 16 75) Similarly, in September 1999, UBS Warburg acted as a co-lead underwriter of Interspeed's
17 IPO and received approximately \$700,000 in investment banking fees as a result.
- 18 76) In October 1999, the analyst initiated coverage on Interspeed with a "Buy" rating and a \$15
19 price target and maintained that position for several months. On January 3, 2000, the Firm's
20 analyst received an e-mail from a junior analyst who asked what to do if Interspeed's annual
21 report reflects inventory and a sales breakout which "differ materially from what we have in
22 the model." The junior analyst also remarked that Interspeed should "get new auditors, their
23 cash flow statement doesn't add up."
- 24 77) That same day, the analyst issued a research report stating the Interspeed had fallen
25 "dramatically short on the top line" in the prior quarter "due to various consumer financing
and delivery issues." Additionally, the analyst issued the "Buy" rating in spite of the fact that
the stock price had risen above the analyst's price target.
- 78) Two days later, on January 5, 2000, the analyst instructed a member of the Firm's sales
force, "Don't put people into Interspeed - very risky." Nevertheless, the analyst maintained
his Buy rating on the stock.
- 79) Approximately 15 minutes later, the recipient of that e-mail replied, asking "so why is ispd
[stock symbol for Interspeed] a short?" The analyst replied, "Just lumpy revenue, some
stuffing of channel, creative accounting."
- 80) The analyst's reference to "customer financing and delivery issues" in his January 3rd report
should have more fully described his concern that Interspeed was suffering from lumpy
revenue or channel stuffing.
- 81) A week after that, on January 11, 2000, the analyst received a question from an institutional
sales force member asking about Interspeed. He responded, "BE CAREFUL about being
long Interspeed. They will report a great number for the December quarter, at least on the
surface of things, but the quality of that number is not necessarily self-evident." (emphasis
in the original).
- 82) On February 4, 2000, the UBS Warburg analyst issued another research report following

1 Interspeed's announcement of its fourth quarter results, which exceeded the analyst's
2 expectations. In that report, the analyst reiterated his "Buy" rating and raising his price
target from \$15 to \$28.

3 83) On March 20, 2000, while the analyst still maintained his "Buy" rating and \$28 price target
4 and with the stock price exceeding that target, the analyst sent an e-mail to UBS Warburg's
sales force informing them that another company had developed a product to compete with
5 Interspeed. One of the members of the sales force responded, "This sounds like a short . . .
correct? (Off the record, of course)." The analyst responded, "YES." However, the analyst
6 still maintained the "Buy" rating.

7 84) On May 31, 2000, the analyst sent an e-mail to two institutional customers saying that "The
two shorts of the group I would suggest are (1) [another issuer] and (2) Interspeed. I'd be
8 wary of shorting any of the others." Nevertheless, the analyst still maintained his "Buy"
rating on Interspeed.

9 85) On July 21, 2000, the analyst dropped the rating on Interspeed from a "Buy" to a "Hold".

10 J. UBS Warburg Received and Made Payments for Research

11 86) UBS Warburg received payments from the lead manager of offerings in which UBS Warburg
did not participate for the issuance of research during the relevant time period.

12 87) During the relevant period, UBS Warburg received a payment of \$100,000 from an outside
13 firm in connection with the offering of Flextronics International, Ltd. The cover letter
enclosing the check indicated that the check was a "special research check." However,
14 UBS Warburg failed to disclose in its research reports concerning Flextronics that it had
received the payment, nor did it disclose the source or amount of the payment.

15 88) During the relevant period, UBS Warburg also received a payment from an outside firm in
the amount of approximately \$113,000 in connection with the offering of Atmel, Inc. The
16 cover letter enclosing the check stated that the check represented "guaranteed economics
for research." However, UBS Warburg failed to disclose in its research reports concerning
17 Atmel that it had received the payment, nor did it disclose the source or amount of the
payment.

18 89) During the relevant period, UBS Warburg also paid a "research fee" of \$150,000 at the
19 direction of the issuer, to two broker-dealers in conjunction with the underwriting transaction
of Netopia, Inc. in which UBS Warburg was the lead-manager. However, UBS Warburg did
20 not take steps to ensure that this broker-dealer disclosed in its research reports that it had
been paid to issue research. Further UBS Warburg did not disclose or cause to be
21 disclosed the details of these payments.

22 90) During the relevant period, UBS Warburg also made several payments totaling
approximately \$283,000, at the direction of the issuer, for "research" to broker-dealers in
23 conjunction with an underwriting transaction of Espeed, Inc., in which UBS Warburg was the
lead manager. However, UBS Warburg did not take steps to ensure that this broker-dealer
24 disclosed in its research reports that it had been paid to issue research. Further UBS
Warburg did not disclose or cause to be disclosed the details of these payments.

25 K. The Firm Failed To Adequately Supervise Its Research and Investment Banking Departments

1 91) While one of the roles of research analysts was to produce objective research, the Firm also
2 encouraged them to participate in investment banking activities. As a result of the
3 foregoing, these analysts were subject to investment banking influences and conflicts of
4 objective research.

5 92) The Firm had knowledge of these investment banking influences and conflicts of interest yet
6 failed to manage them adequately to protect the objectivity of its published research.

7 93) The Firm failed to establish and maintain adequate policies, systems and procedures
8 reasonably designed to ensure the objectivity of its published research. Although the Firm
9 had some policies governing research analyst activities during the relevant period, these
10 policies were not adequate to fully address the conflicts of interest that existed.

11 II.

12 CONCLUSIONS OF LAW:

13 1) The Alaska division of banking, securities, and corporations (division) has jurisdiction over
14 this matter pursuant to the Alaska Securities Act (Act).

15 2) The division finds that the Firm violated AS 45.55.060(a)(7) by:

- 16 • engaging in the acts and practices that created or maintained inappropriate
17 influence by the Investment Banking Department over research analysts, therefore
18 imposing conflicts of interest on its research analysts, and failing to manage these
19 conflicts in an adequate or appropriate manner;
- 20 • issuing research reports that were affected by the conflicts of interest imposed on
21 its research analysts as described above;
- 22 • making payments for research to other broker-dealers not involved in underwriting
23 transactions when the Firm knew that these payments were made, at least in part,
24 for research coverage, and by failing to disclose or cause to be disclosed in
25 offering documents or elsewhere the fact of such payments; and
- receiving payments in conjunction with underwriting transactions from outside
entities for research issued without disclosing receipt of those payments to the
public as required by Section 17(b) of the Securities Act of 1933, as amended.

3) The Firm violated AS 45.55.060(b)(1) by failing to establish and maintain adequate policies,
systems and procedures for supervision and control of the Research and Investment
Banking Departments reasonably designed to detect and prevent the foregoing investment
banking influences and manage the conflicts of interest to assure compliance with
applicable securities laws and regulations.

4) The division finds the following relief appropriate and in the public interest.

III.

ORDER

On the basis of the Findings of Fact, Conclusions of Law, and UBS Warburg's and UBS
PaineWebber's consent to the entry of this Order, for the sole purpose of settling this matter, prior
to a hearing and without admitting or denying any of the Findings of Fact or Conclusions of Law,

IT IS HEREBY ORDERED:

1) This Order concludes the investigation by the division and any other action that the division
could commence under applicable Alaska law on behalf of the State of Alaska as it relates to

1 the Firm, relating to certain research practices at the Firm described herein.

2 2) The Firm will CEASE AND DESIST from violating the Act at AS 45.55.060(a)(7) and (b)(1) in
3 connection with the research practices referenced in this Order, will comply with AS
4 45.55.060(a)(7) and (b)(1) in connection with the research practices referenced in this Order,
5 and will comply with the undertakings of Addendum A, incorporated herein by reference.

6 3) As a result of the Findings of Fact and Conclusions of Law contained in this Order, the Firm
7 shall pay a total amount of \$80,000,000.00. This total amount shall be paid as specified in
8 the SEC Final Judgment as follows:

- 9 • \$25,000,000 to the states (50 states, plus the District of Columbia and Puerto Rico)
10 (the Firm's offer to the state securities regulators hereinafter shall be called the "state
11 settlement offer"). Upon execution of this Order, the Firm shall pay the sum of
12 \$250,000 of this amount to the State of Alaska as a civil monetary penalty pursuant
13 to the agreement of the parties, to be deposited in the general fund. The total
14 amount to be paid by the Firm to state securities regulators pursuant to the state
15 settlement offer may be reduced due to the decision of any state securities regulator
16 not to accept the state settlement offer. In the event another state securities
17 regulator determines not to accept the Firm's state settlement offer, the total amount
18 of the Alaska payment shall not be affected, and shall remain at \$250,000;
- 19 • \$25,000,000 as disgorgement of commissions, fees and other monies as specified in
20 the SEC Final Judgment;
- 21 • \$25,000,000, to be used for the procurement of independent research, as described
22 in the SEC Final Judgment;
- 23 • \$5,000,000, to be used for investor education, as described in Addendum A,
24 incorporated by reference herein.

25 4) If payment is not made by the Firm or if the Firm defaults in any of its obligations set forth in
this Order, the division may vacate this Order, at its sole discretion, upon 10 days notice to
the Firm and without opportunity for administrative hearing.

5) The Firm agrees that it shall not seek or accept, directly or indirectly, reimbursement or
indemnification, including but not limited to payment made pursuant to any insurance policy,
with regard to all penalty amounts that the Firm shall pay pursuant to this Order or section II
of the SEC Final Judgment, regardless of whether such penalty amounts or any part thereof
are added to the Distribution Fund Account referred to in the SEC Final Judgment or
otherwise used for the benefit of investors. The Firm further agrees that it shall not claim,
assert, or apply for a tax deduction or tax credit with regard to any state, federal or local tax
for any penalty amounts that the Firm shall pay pursuant to this Order or section II of the
SEC Final Judgment, regardless of whether such penalty amounts or any part thereof are
added to the Distribution Fund Account referred to in the SEC Final Judgment or otherwise
used for the benefit of investors. The Firm understands and acknowledges that these
provisions are not intended to imply that the State of Alaska would agree that any other
amounts the Firm shall pay pursuant to the SEC Final Judgment may be reimbursed or
indemnified (whether pursuant to an insurance policy or otherwise) under applicable law or
may be the basis for any tax deduction or tax credit with regard to any state, federal or local
tax.

6) This Order is not intended by the division to subject any Covered Person to any
disqualifications under the laws of any state, the District of Columbia or Puerto Rico
(collectively, "State"), including, without limitation, any disqualifications from relying upon the
State registration exemptions or State safe harbor provisions. "Covered Person" means the
Firm, or any of its officers, directors, affiliates, current or former employees, or other person

- 1 that would otherwise be disqualified as a result of the Orders (as defined below).
2 7) The SEC Final Judgment, the NYSE Stipulation and Consent, the NASD Letter of
3 Acceptance, Waiver and Consent, this Order and the order of any other State in related
4 proceedings against the Firm (collectively, the "Orders") shall not disqualify any Covered
5 Person from any business that they otherwise are qualified, licensed or permitted to perform
6 under the applicable law of Alaska and any disqualifications from relying upon this state's
7 registration exemptions or safe harbor provisions that arise from the Orders are hereby
8 waived.
- 9 8) The Orders shall not disqualify any Covered Person from any business that they otherwise
10 are qualified, licensed or permitted to perform under applicable state law.
- 11 9) For any person or entity not a party to this Order, this Order does not limit or create any private
12 rights or remedies against the Firm including, without limitation, the use of any e-mails or other
13 documents of the Firm or of others regarding research practices, or limit or create liability of the
14 Firm, or limit or create defenses of the Firm to any claims.
- 15 10) Nothing herein shall preclude the State of Alaska, its departments, agencies, boards,
16 commissions, authorities, political subdivisions and corporations, other than the division and
17 only to the extent set forth in paragraph 1 above, (collectively, "State Entities") and the
18 officers, agents or employees of State Entities from asserting any claims, causes of action,
19 or applications for compensatory, nominal and/or punitive damages, administrative, civil,
20 criminal, or injunctive relief against the Firm in connection with certain research practices at
21 the Firm.

22 BY ORDER OF THE ADMINISTRATOR OF SECURITIES.

23 Dated this 29 day of August, 2003.

24 /s/ Mark R. Davis
25 Mark R. Davis
Administrator of Securities