

NASD
LETTER OF ACCEPTANCE, WAIVER AND CONSENT
NO. CAF030022

TO: Department of Enforcement
NASD

RE: UBS Warburg LLC, Respondent, CRD No. 7654

Pursuant to Rule 9216 of the NASD Code of Procedure, Respondent UBS Warburg LLC (together with its predecessor firms "Respondent" 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 in Part II below. This AWC is submitted on the condition that, if accepted, NASD will not bring any future actions against Respondent alleging violations based on the same factual findings.

Respondent understands that:

1. Submission of this AWC is voluntary and will not resolve this matter unless and until it has been reviewed and accepted by NASD's Department of Enforcement and National Adjudicatory Council ("NAC"), pursuant to NASD Rule 9216;
2. If this AWC is not accepted, its submission will not be used as evidence to prove any of the allegations against Respondent; and
3. If accepted:
 - a. this AWC will become part of Respondent's permanent disciplinary record and may be considered in any future actions brought by NASD or any other regulator against Respondent;
 - b. this AWC will be made available through NASD's public disclosure program in response to public inquiries about Respondent's disciplinary record;
 - c. NASD may make a public announcement concerning this agreement and the subject matter thereof in accordance with NASD Rule 8310 and IM-8310-2; and
 - d. Respondent 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 allegation in this AWC or creating the impression that the AWC is without

factual basis. Nothing in this provision affects the testimonial obligations or right of Respondent to take legal or factual positions in litigation or other legal proceedings in which NASD is not a party.

Respondent also understands that its experience in the securities industry and disciplinary history may be factors that will be considered in deciding whether to accept this AWC:

Respondent has been a member of NASD since 1978. It is principally owned by UBS AG and is engaged in the business of global investment banking and securities. Respondent also provides services on a worldwide basis, including investment banking, securities trading and principal investments, and asset management. Respondent's principal office is located at 677 Washington Boulevard, in Stamford, Connecticut.

UBS AG purchased PaineWebber Inc. ("PaineWebber") in November 2000 and PaineWebber became known as UBS PaineWebber. PaineWebber, founded in 1879, was a full-service securities firm located in New York and has been a member of NASD since 1936. As part of the merger, PaineWebber's banking and research activities were shifted to UBS Warburg LLC, and some investment bankers and research analysts previously employed by PaineWebber became employees of UBS Warburg LLC. Since the merger, UBS PaineWebber is principally engaged in the business of servicing retail investors and no longer employs equity investment bankers or research analysts. UBS PaineWebber's principal office is located at 1285 Avenue of the Americas, New York, New York.

Neither PaineWebber, UBS PaineWebber nor UBS Warburg LLC has any relevant disciplinary history.

In this AWC, PaineWebber, UBS PaineWebber and UBS Warburg LLC are collectively referred to as the "Respondent" or the "Firm" except when PaineWebber, UBS PaineWebber or UBS Warburg LLC are specifically referenced.

I.

WAIVER OF PROCEDURAL RIGHTS

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

- A. To have a Formal Complaint issued specifying the allegations against it;
- 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 NAC and then to the U.S. Securities and Exchange Commission ("Commission") and a U.S. Court of Appeals.

Further, Respondent specifically and voluntarily waives any right to claim bias or prejudice 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 Rule 9143 or the separation of functions prohibitions of 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.

II.

ACCEPTANCE AND CONSENT

Respondent hereby accepts and consents, without admitting or denying the allegations or findings, and solely for the purposes of this proceeding and any other proceeding brought by or on behalf of NASD, or to which NASD 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 NASD:

A. Overview

This action concerns the research and investment banking activities at UBS Warburg LLC during the period July 1, 1999 through June 30, 2001 (the "relevant period") as well as the research and investment banking activities at PaineWebber from July 1, 1999 until its merger with UBS AG on November 3, 2000.

During the relevant period, as set forth below, the Firm sought and did investment banking business with many companies covered by the Firm's Research Department. Research analysts were encouraged to participate in investment banking activities and that was a factor considered in the analysts' compensation. In addition, the decision to initiate and maintain research coverage of certain companies was in some cases coordinated with the Investment Banking Department and influenced by investment banking interests.

As a result of the foregoing, as set forth below, certain research analysts at the Firm were subject to investment banking influences and conflicts of interest between supporting the investment banking business at the Firm and publishing objective research.

As set forth below, the Firm had knowledge of these investment banking influences and 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 and manage those conflicts.

B. The Role of the Research Analyst

Research analysts were responsible for providing analyses of the financial outlook of particular companies in the context of the business sectors in which those companies operate and the securities markets as a whole.

The Firm publishes research on publicly traded companies based upon analysts' examining, among other things, financial information contained in public filings, questioning company management, investigating customer and supplier relationships, evaluating companies' business plans and the products or services offered, building financial models, and analyzing competitive trends.

After synthesizing and analyzing this information, analysts produced research in the form of 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. 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 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 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 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. These summaries did not include any of the analyses contained in the actual research reports.

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 ("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.

Nevertheless, analysts were sometimes able to upgrade or downgrade ratings by requesting 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 was based upon breaking news. Because the Firm's analysts sometimes changed their ratings based upon breaking news, upgrades or downgrades were authorized without the approval of the full IRC in nearly one-third of the instances in which ratings were changed during the Relevant Period.

Analysts also made themselves available to the Firm's institutional and retail sales force to 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-mails and voice messages, which typically provide a rating and a more abbreviated analysis than what is contained in a research report.

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

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

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

C. Research Analyst Participation in Investment Banking Activities

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

During the relevant period, investment banking was an important source of revenues and profits for UBS Warburg. UBS Warburg's investment banking department reported global 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.

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

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.

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

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

D. Participation in Investment Banking Activities was a Factor in Evaluating and Compensating Research Analysts

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

The performance of research analysts was evaluated by Research Management through an annual review process and analysts' bonuses were determined through this process, unless an analyst had a guaranteed bonus set

by contract in advance. The guaranteed bonuses for the Firm's top analysts were frequently in the millions of dollars while the base salary was typically in the \$125,000 to \$150,000 range.

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

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

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

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

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

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

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

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

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

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

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

E. Investment Banking Interests Influenced the Firm's Decisions to Initiate and Maintain Research Coverage

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

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

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

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.

Additionally, according to an e-mail by UBS Warburg's Head of Global Technology Investment Banking, it was an implicit condition in UBS Warburg's 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.

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.

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

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

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

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

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

F. The Firm's Pitch Materials Contained Discussions of Research Coverage

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

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.

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, the Firm's 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.

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.

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.

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.

The pitch books contained information relating to the company, its competition, the sector in which it operated and the nature of the services the Firm could provide to the company and its shareholders after the completion of a potential offering. Additionally, the Firm's pitch books sometimes contained implicit representations that the Firm would continue to provide service to the issuer after the offering by providing research coverage about the company.

Some pitch books contained information indicating that a specific analyst would cover the company and included data demonstrating how that analyst's positive comments about other companies in the sector had had a direct positive impact upon the stock prices of those companies.

For example, the pitch book presented to JDS Uniphase by PaineWebber, discussed the impact that PaineWebber research had on covered stocks by

including a graphic depicting the performance of stocks on PaineWebber's "Buy List" as opposed to stocks on PaineWebber's "Attractive List" and "Neutral List." At the top of the graphic, PaineWebber quoted a report from Reuters which stated, "Shares of semiconductor companies specializing in chips for the communications market rose on Thursday after PaineWebber published a report citing the sector's growth prospects."

Similarly, in a pitch book presented to Avant Immunotherapeutics, Inc., PaineWebber presented a slide entitled "Demonstrated Strength in Equity Trading and Research." One of the sub-topics on the slide stated, "Buy and attractive recommendations have outperformed the S&P 500 by 84 percentage points for the period 1/90 through 12/99" while "Sell and unattractive ratings have underperformed the S&P 500 by 361 percentage points for the period 1/90 through 12/99."

Because analysts often participated in the Firm's efforts to win investment banking business, analysts were sometimes subjected to competing pressures after a stock became publicly 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.

G. Research Analysts Rarely Issued Neutral or Negative Ratings

During the relevant period, PaineWebber's rating system allowed research analysts to assign one of four ratings to a stock: "Buy", defined as total return expected to exceed that of the S&P 500 by 20 percentage points or more over the next 12 months; "Attractive", 12 month total return potential that is 10-20 percentage points greater than the market's; "Neutral", 12 month total return potential within 10 percentage points of the market's; "Unattractive", expected to underperform the market by more than 10 percentage points on a total return basis over the next 12 months.

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.

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

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

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

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

H. In Certain Instances, the Firm Published Exaggerated or Unwarranted Research

On several occasions, the conflicts of interest discussed above resulted in analysts publishing ratings and/or recommendations that violated the NASD Advertising Rules (Conduct Rule 2210). The following are examples of how these conflicts affected the research.

1. Triangle Pharmaceuticals

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.

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.

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.

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.

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.”

The analyst spoke to the UBS Warburg sales force before the market opened following Triangle’s announcement of the FDA’s decision and made a statement in form or in substance that the FDA’s action had been an anticipated possibility notwithstanding the analyst’s “Buy” rating on the stock.

Following that call, a member of UBS Warburg’s Equity Trading Management contacted the analyst by e-mail and expressed disappointment that the analyst anticipated that the FDA might take this action but had failed to adequately emphasize that possibility to the sales force.

The analyst responded that her failure to emphasize negative information regarding Triangle was, at least partially, a result of the analyst’s allegiance to the investment banking client: “Triangle is a very important client of the firm. We could not go out with a big research call trashing their lead product, although we had a feeling the FDA might balk. Had we been right or wrong, it would have been a disaster. I just wanted the salesforce to know we were not surprised, and that where appropriate we had had some conversations with the buy-side. Sorry this was not conveyed.”

2. Interspeed

Similarly, in September 1999, UBS Warburg acted as a co-lead underwriter of Interspeed’s IPO and received approximately \$700,000 in investment banking fees as a result.

In October 1999, the analyst initiated coverage on Interspeed with a “Buy” rating and a \$15 price target and maintained that position for several months. On January 3, 2000, the analyst received an e-mail from a junior analyst who asked what to do if Interspeed’s annual report reflects inventory and a sales breakout

which “differ materially from what we have in the model.” The junior analyst also remarked that Interspeed should “get new auditors, their cash flow statement doesn’t add up.”

That same day, the analyst issued a research report stating that Interspeed had fallen “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.

Two days later, on January 5, 2000, the analyst instructed a member of Warburg’s sales force, “Don’t put people into Interspeed – very risky.” Nevertheless, the analyst maintained his Buy rating on the stock.

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.”

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.

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).

On February 4, 2000, the UBS Warburg analyst issued another research report following Interspeed’s announcement of its fourth quarter results, which exceeded the analyst’s expectations. In that report, the analyst reiterated his “Buy” rating and raised his price target from \$15 to \$28.

On March 20, 2000, while the analyst still maintained his “Buy” rating and \$28 price target and with the stock price exceeding that target, the analyst sent an e-mail to the UBS Warburg sales force informing them that another company had developed a product to compete with 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 still maintained the “Buy” rating.

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 wary of shorting any of the others.” Nevertheless, the analyst still maintained his “Buy” rating on Interspeed.

On July 21, 2000, the analyst dropped the rating on Interspeed from a “Buy” to a “Hold”.

I. UBS Warburg Received and Made Payments for Research

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.

During the relevant period, UBS Warburg received a payment of \$100,000 from an outside 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, 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.

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 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 Atmel that it had received the payment, nor did it disclose the source or amount of the payment.

During the relevant period, UBS Warburg also paid a “research fee” of \$150,000 at the 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 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 disclosed the details of these payments.

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 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 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.

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

While one of the roles of research analysts was to produce objective research, the Firm also encouraged them to participate in investment banking activities. As a result of the foregoing, these analysts were subject to investment

banking influences and conflicts of interest between supporting the Firm's investment banking business and publishing objective research.

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

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

K. Violations

Violation of NASD Conduct Rules Due to Conflicts of Interest Resulting from Investment Banking Influence over Research Analysts. NASD Conduct Rule 2110 requires that member firms observe high standards of commercial honor and just and equitable principles of trade. As described above, the Firm engaged in the acts and practices that created and/or maintained inappropriate influence by the Investment Banking Department over research analysts and therefore imposed conflicts of interest on its research analysts. The Firm failed to manage these conflicts in an adequate or appropriate manner. Accordingly, the Firm violated NASD Conduct Rule 2110.

Violation of NASD Conduct Rules by Publishing Research that Was Exaggerated or Unwarranted. NASD Conduct Rule 2210, in part, prohibits members from making exaggerated or unwarranted claims in public communications and requires members to have a reasonable basis for all recommendations made in advertisements and sales literature. As described above, the Firm issued certain research reports on companies that were not based on principles of fair dealing and good faith and did not provide a sound basis for evaluating facts, contained exaggerated or unwarranted claims about these companies, and/or contained opinions for which there was no reasonable basis. Accordingly, the Firm violated NASD Conduct Rules 2110, 2210(d)(1), and 2210(d)(2).

Violation of NASD Conduct Rules by Receiving and Not Disclosing Payments for Initiating Research. Section 17(b) of the Securities Act of 1933 [15 U.S.C. § 77q(b)] states:

It shall be unlawful for any person, by the use of any means or instruments of transportation or communication in interstate commerce or by the use of the mails, to publish, give publicity to, or circulate any notice, circular, advertisement, newspaper, article, letter, investment service, or communication which, though not

purporting to offer a security for sale, describes such security for a consideration received or to be received, directly or indirectly, from an issuer, underwriter, or dealer, without fully disclosing the receipt, whether past or prospective, of such consideration and the amount thereof.

As described above, the Firm received payments in conjunction with an underwriting from outside entities for research without disclosing receipt of that payment to the public. Accordingly, the Firm failed to comply with the requirements of Section 17(b) and violated NASD Conduct Rules 2110 and 2210(d)(1)(A).

Violation of NASD Conduct Rule by Paying Underwriting Fees to Other Broker-Dealers for Research. As described above, the Firm made payments for research to other broker-dealers not involved in an underwriting transaction, when the Firm knew that these payments were made, at least in part, for research coverage, and failed to disclose or cause to be disclosed in offering documents or elsewhere the fact of such payments. By reason of the foregoing, the Firm violated NASD Conduct Rules 2110 and 2210(d)(1)(A).

Violation of NASD Conduct Rules by Failing to Supervise. NASD Conduct Rule 3010(a) requires members, among other things, to “establish and maintain a system to supervise the activities of each registered representative and associated person that is reasonably designed to achieve compliance with applicable securities laws and regulations, and with” NASD’s own Rules. As described above, during the relevant time period, the Firm failed 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, including a separate system of follow-up and review to assure compliance with applicable NASD Conduct Rules. By reason of the foregoing, the Firm violated NASD Conduct Rule 3010(a).

L. Sanctions

The Firm consents to the imposition, at a maximum, of the following sanctions:

1. a censure; and
2. a total payment of \$80,000,000.00, as specified in the Final Judgment ordered in a related action filed by the Securities and Exchange Commission (“Final Judgment”), as follows:
 - (a) \$25,000,000, as a fine;

- (b) \$25,000,000, as disgorgement of commissions, fees, and other monies;
- (c) \$25,000,000, to be used for the procurement of Independent Research, as described in Addendum A: Undertakings to the Final Judgment ("Addendum A"); and
- (d) \$5,000,000, to be used for investor education, as described in the Final Judgment.

The monetary sanctions imposed by NASD shall be reduced by the amounts paid by Respondent pursuant to the Final Judgment. Addendum A and the payment provisions of the Final Judgment are incorporated herein by reference.

Respondent 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 fine/penalty amounts that Respondent shall pay pursuant to Section II of the Final Judgment, regardless of whether such fine/penalty amounts or any part thereof are added to the Distribution Fund Account or otherwise used for the benefit of investors. Respondent further agrees that it shall not claim, assert, or apply for a tax deduction or tax credit with regard to any federal, state, or local tax for any fine/penalty amounts that Respondent shall pay pursuant to Section II of the Final Judgment, regardless of whether such fine/penalty amounts or any part thereof are added to the Distribution Fund Account or otherwise used for the benefit of investors. Respondent understands and acknowledges that these provisions are not intended to imply that NASD would agree that any other amounts Respondent shall pay pursuant to the 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 federal, state, or local tax.

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


III.

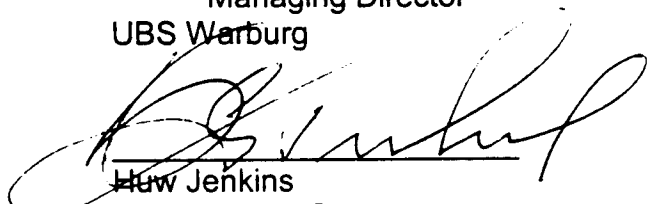
OTHER MATTERS

Respondent understands that it may attach a Corrective Action Statement to this AWC that is a statement of demonstrable corrective steps taken to prevent future misconduct. It 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 NASD, nor does it reflect the views of NASD or its staff.


Respondent certifies that it has read and understands all of the provisions of this AWC and has been given a full opportunity to ask questions about it, and that no offer, threat, inducement, or promise of any kind, other than the terms set forth herein, has been made to induce Respondent to submit it.

UBS WARBURG LLC


Robert C. Dinerstein
Global General Counsel and
Managing Director
UBS Warburg


Huw Jenkins
Managing Director
UBS Warburg

Reviewed by:



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One Liberty Plaza
New York, New York 10006
Attorneys for UBS Warburg LLC

Date: April 21, 2003

Accepted by NASD:

On behalf of the Director of the Office of
Disciplinary Affairs, through delegated
authority,

4/24/03
Date


Barry R. Goldsmith
Executive Vice President
Department of Enforcement
NASD
1801 K St. NW
Washington, DC 20006