

# Barrier options disclosure

Investment bank



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**This updated barrier option disclosure document amends and supersedes any previous communication we have sent to you in respect of barrier options. You should read and understand this document as it describes the method and process by which we will determine whether a barrier event has occurred in respect of any relevant transaction you entered into with us.<sup>1</sup>**

Barrier options are complex instruments with unusual risks. We view any barrier option you enter into with us as an arm's length transaction, and we assume that you have taken adequate steps to inform yourself of the characteristics of barrier options and the barrier options market. The following are UBS's practices with respect to barrier options.

If you have any questions, we would be happy to discuss them with you.

## 1 Barrier options

- (a) UBS defines a barrier option as an option the terms of which change in some pre-defined manner when a barrier event occurs. A **"barrier event"** is a transaction in the relevant currency pair (for the avoidance of doubt, 'currency pair' in this document includes Precious Metals) occurring in the spot market at a rate that is at or beyond a certain pre-specified level (generically called the **"barrier price"**).
- (b) For example, a knock-out option is one that terminates before its scheduled expiration if a spot transaction occurs that is at or beyond the out-strike price.
- (c) There are many specific types of barrier options, including the knock-out option, the double knock-out option, the knock-in option, the no-touch option, the double no-touch option, the one-touch option, the step payment option and others. In particular cases, the barrier price may be called the out-strike price, the in-strike price, the trigger price, etc., depending on the type of barrier option.
- (V) transactions that are known to UBS at the time of determination to be cancelled, voided or amended/rebooked at a price that does not breach the applicable barrier; and
- (D) **must be of "commercial size"**: in liquid markets, a commercial size is a minimum of USD3 million (or equivalent) (which could comprise two or more substantially contemporaneous transactions). UBS may use a transaction below USD3 million (or equivalent) for illiquid currency pairs or in illiquid markets or other extraordinary market circumstances.
- (ii) **Timing of Determination**: If UBS is aware that or reasonably believes that there may be further information which may become available which may have an impact on its determination, such as there being a transaction which may breach a barrier being under discussion with a view to it being amended, rebooked, cancelled or voided, UBS may delay its determination in order to obtain further information.
- (iii) **Illiquid Currency Pairs**: UBS may use cross-currency rates to determine whether a barrier event has occurred in respect of a currency pair that is not commonly quoted. UBS may use two or more substantially contemporaneous transactions in the most liquid applicable currency pairs to calculate the cross rate.

## 2 Declaration of a barrier event

UBS, acting as barrier determination agent, will declare whether a barrier event has occurred for the purposes of the Transaction in good faith and a commercially reasonable manner taking the following factors into consideration:

- (i) **Eligible Transactions**: Where UBS is considering whether any transactions breach a barrier, the relevant transactions:
  - (A) **must be** evidenced by information available on or from an electronic broker service;
  - (B) **may include** transactions to which UBS is a party;
  - (C) **shall not include**:
    - (I) non-arm's length transactions;
    - (II) quotations;
    - (III) transactions that UBS is not able to observe from sources available to it in the ordinary course of its business;
    - (IV) transactions at off-market prices (defined as a rate more favorable or less favorable than the rate available to a professional spot dealer in the interbank spot market at the time of the transaction); or

## 3 A barrier event does not require the execution of a specific order

A barrier event does not require the execution of an order placed by the seller or the buyer of the option at the barrier price. A barrier event is simply a transaction meeting the criteria set out in Section 2 above. It is thus possible for a barrier event to occur even though an order placed by you or by UBS at the Barrier Price remains unfilled.

## 4 UBS generally hedges its barrier option positions

UBS generally hedges its barrier option positions with spot, forwards and options, though it may not always do so. UBS reserves the right to leave a barrier option position unhedged, partially hedged or fully hedged, and to adjust the hedge from time to time in any manner it sees fit.

<sup>1</sup> Assuming entered into after 1 May 2017

**5 UBS may unwind its hedge in anticipation of a barrier event**

If UBS has decided to maintain a spot hedge on a barrier option position, it will need to unwind the spot hedge when a barrier event occurs. Unwinding the hedge typically consists of buying or selling a quantity of the currency to which UBS is exposed, thereby flattening its position. It may not be possible to unwind a hedge in a single transaction timed to coincide with the barrier event. In order to achieve an average fill as close to the barrier price as possible, UBS may therefore at times anticipate the barrier event and begin unwinding its hedge before the barrier event occurs. This activity may affect the probability that a barrier event will occur.

**6 UBS is an active participant in the interbank spot and option market**

UBS is an active participant in the interbank spot and option market as a principal market maker and riskless principal for its customers, and therefore at any given time it may be engaging in currency or currency derivative transactions. Such transactions may affect the probability that a barrier event will occur.

**7 UBS does not act as adviser to its barrier option clients**

While UBS provides its clients with information and explanations as to the terms and conditions of barrier options, it does not act as a fiduciary for or an adviser to its barrier option clients. No communication from UBS should be construed as investment advice, or as a recommendation to enter into any barrier option, or as an assurance or guarantee as to the expected results of a barrier option.