3.41.2 SWITZERLAND – CONTRACTUAL LAW BASED COVERED BONDS

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I. FRAMEWORK

In 2009 and 2010 respectively, UBS AG (UBS) and Credit Suisse AG (Credit Suisse) established contractual covered bond programmes in order to access covered bond funding in the EUR and USD markets. The UBS and Credit Suisse programmes use Swiss and English law contractual provisions to implement structural features that are standard in the covered bond market. However, in response to evolving regulatory environment and to comply with the Swiss "too big to fail" requirements, Credit Suisse and UBS have since implemented changes to their legal entity structures. Among the required changes were the establishment of new Swiss banking subsidiaries intended to hold (among other businesses) their retail mortgage businesses. These changes necessitated structural changes to the covered bond programmes which UBS and Credit Suisse implemented in June 2015 and November 2016, respectively. Following these changes, Credit Suisse and UBS no longer issue covered bonds out of these programmes.

Starting in 2017, new contractual covered bond programmes were established by Valiant Bank AG (Valiant), Credit Suisse (Schweiz) AG (CS Schweiz), Crédit Agricole next bank (Suisse) SA (CAnb) and Cornèr Bank SA (Cornèr Bank) in order to diversify their funding sources. As with UBS and Credit Suisse legacy covered bond programmes, these are structured programmes that are not subject to the Swiss Pfandbriefe legislation. However, in contrast to UBS and Credit Suisse's legacy programmes, all of these programmes exclusively use Swiss law provisions and had so far only issued CHF-denominated series until 2022 when CS Schweiz issued its first EUR-denominated Swiss contractual law covered bond in the form of its EUR 750m 3-year covered bond in October 2022.

II. STRUCTURE OF THE ISSUER

In line with the guarantor Special Purpose Vehicle (SPV) model used in the United Kingdom and the Netherlands (among other jurisdictions), the issuers have established Swiss based special purpose companies to guarantee their payment obligations for the benefit of the covered bondholders. All programmes feature direct recourse to the issuer, which remains primarily responsible for payments on the bonds. These guarantor entities hold security over the programmes' respective cover pools and may use the cover pool assets to make payments on the covered bonds should the issuer fail to do so. In case of Valiant, in addition to mortgage claims, the covered bondholders benefit from accessory preferential claims pledged by the mortgagor for the benefit of the issuer and transferred to the guarantor by way of security. The guarantee comes into operation following an issuer event of default, subject to certain conditions. All covered bonds issued under the respective programmes rank *pari passu* with each other and benefit equally from the guarantee. The guarantors are ring-fenced, bankruptcy-remote entities designed to be unaffected by the insolvency of the group to which they are consolidated (guarantors are majority-owned by their respective issuer). All issuers are financial institutions regulated by the Swiss banking regulator, the Swiss Financial Market Supervisory Authority (FINMA).

As part of their legal entity restructurings, UBS and Credit Suisse transferred their residential mortgage businesses to UBS Switzerland AG and CS Schweiz AG, their newly established domestic subsidiaries. Concurrently, joint and several liability arrangements were put in place under which these subsidiaries assumed joint and several liability for all contractual obligations of the issuers under the programme, including the covered bonds themselves.

III. COVER ASSETS

The collateral of Swiss contractual law based covered bonds consists of Swiss residential mortgage loans to private individuals and the related mortgage certificates securing such mortgage loans. In case of Valiant, in

addition to mortgage claims, the covered bondholders benefit from accessory preferential claims pledged by the mortgagor for the benefit of the issuer and transferred to the guarantor by way of security. The accessory preferential claims are second and third pillar pension fund assets and are not taken into account in the cover pool and in the calculation of the asset coverage test. Substitution assets can also be used as collateral of the covered bonds as long as their aggregate value does not exceed 15% of the cover pool. They comprise deposits in CHF (foreign currencies eligible only for hedging purpose) and authorised investments. The latter need to comply with stringent ratings to be cover pool eligible.

IV. VALUATION AND LTV CRITERIA

The eligibility criteria for initial inclusion in the Credit Suisse, CS Schweiz, CAnb and Cornèr Bank cover pool limit mortgages to those with a loan-to-value (LTV) of less than or equal to 100%, while the UBS and Valiant programmes limit eligible mortgages to those with LTV of less than or equal to 80%. Certain provisions within the programmes' asset coverage test (ACT) implement LTV limits by capping the value of each mortgage loan at a specified current LTV. This limit is 70% LTV in the Credit Suisse programme and 80% in the CS Schweiz, UBS, Valiant, CAnb and Cornèr Bank programmes (for mortgage loans on eligible residential properties) and a limit of 60% for mortgage loans on eligible commercial properties under the Cornèr Bank programme

Mortgage LTVs are regularly calculated using current market values. In case of both Credit Suisse and Valiant programmes, appraisals are undertaken for each mortgage loan application by a valuation model (the IAZI). This comparative approach is one of the main methods used for the appraisal of real estate properties in Switzerland. The property is compared with thousands of other objects previously sold on the market. The price of the object is statistically estimated by comparing the price of properties with similar attributes in comparable locations. The credit risk management department, responsible for the continuous monitoring of the bank's mortgage portfolio, has the discretionary power to trigger a revaluation based on its analysis outcomes. UBS and CAnb conduct similar estimations of the collateral value for residential mortgages based on the Wüest & Partner valuation model, which is also a hedonic regression model. Other valuation methods may be used at the discretion of the lenders in specific circumstances and taken into consideration.

V. ASSET – LIABILITY MANAGEMEMT

The ACT determines whether the value of the cover pool assets is sufficient for the timely payment of capital and interest owed under the covered bonds and confirms that the minimum overcollateralization (OC) requirements are met. The test is carried out monthly and the results are disclosed in the investor reporting. In addition to the LTV limitations described above, a second part of the ACT haircuts the full balance of the mortgages using an asset percentage (AP). The AP is derived from periodic rating agency feedback and sized to maintain a triple-A rating. The value given to the mortgage assets under the ACT is the lower of (i) the result when applying the LTV limits described above or (ii) the value of the mortgage assets multiplied by the AP. In addition, credit is given to cash and substitute assets while further deductions are made for loans in arrears, borrower set-off risk and potential negative carry. The resulting value must be equal to or exceed the value of the covered bonds outstanding for the test to be passed.

The APs in UBS, Credit Suisse, CS Schweiz, CAnb and Cornèr Bank programmes may fluctuate over time, but are constrained by a maximum value. Valiant uses an alternative ACT ("Aktivendeckungstest"), including a minimum OC. The adjusted value of the Valiant cover pool always has to be equal to at least the nominal value of the outstand ing covered bonds including a minimum OC, corresponding to the OC required to maintain the actual ratings up to a maximum committed level capped by contractual provisions at 50%.

The Swiss contractual law covered bond programmes benefit from additional safeguards:

> Exposure to interest rate and currency risks are mitigated by use of derivatives in the UBS programme, legacy Credit Suisse and CS Schweiz programme. In case of Valiant and CAnb, the option to implement derivative instruments is available but has not been to date.

> Liquidity risk is mitigated by the requirements to establish reserve funds, pass an interest coverage test (ICT), maintain pre-maturity liquidity (for hard bullet covered bonds) and the inclusion of 12-months extension periods (for soft bullet covered bonds). In case of Valiant, the soft bullet structure may not only be applied to a covered bond series after an issuer event of default but may also applied to all outstanding covered bond series after a guarantor event of default (to reduce fire sale risk).

> Minimum rating requirements are in place for the third parties that support the transaction, including the account bank, corporate services provider, servicer and cash manager.

> Commingling risk is mitigated by the requirement of all collections arising from the cover pool assets to be transferred into guarantor cover pool bank account after a specific rating downgrade of the issuer.

> Independent audits of the calculations undertaken on a regular basis by a cover pool monitor.

Upon an issuer event of default following the service of a notice to pay, the Amortisation Test (AT) is run on each calculation date instead of the ACT, and the ICT is no longer run. The AT is similar to the ACT and is designed to mitigate time subordination between the covered bond series therefore ensuring that the cover pool will be sufficient to make payments as required under the guarantee. Upon failure of the test, all covered bonds accelerate against the guarantor.

VI. TRANSPARENCY

The issuers have committed to publishing monthly investor reports on a timely basis. These reports provide information relevant to investors including:

> The monthly calculations of the ACT and the ICT.

> Details of outstanding covered bonds and list of parties involved in the transaction.

> The current balance of programme accounts.

> A mortgage portfolio summary disclosing total balances, average loan balance, number of properties, WA remaining terms and WA LTVs.

> Tables showing number properties and mortgages by remaining term, current LTV, total balance, interest rate type, property region, property type, and arrears.

VII. COVER POOL MONITOR AND BANKING SUPERVISION

The issuers are regulated Swiss financial institutions, which are subject to regulation and supervision by FINMA. The cover pool tests comprising the ACT and the ICT as well as AT in case of an issuer's event of default, are checked and verified on a regular basis by an independent cover pool monitor. The results of his review are summarised in cover pool monitor reports for the attention of the guarantor, the issuer and the administrator. The administrator, independent from the issuer, has the duty to advise the bondholder representative (trustee) inter alia upon the breach of a cover pool test. The administrator is responsible for an ongoing monitoring of the cover pool. His main task comprises confirming the accuracy of the inclusion in or the removal from the cover pool, inter alia ensuring that the eligibility criteria are met and verifying that the registered amount in the cover pool is correct. In order to constitute a valid security interest the issuer will no longer be able to dispose over the mortgage certificates by its sole acts. The mortgage certificates can only be accessed with the presence and approbation of the administrator. In addition, rating agencies regularly monitor the programme.

VIII. SEGREGATION OF COVER ASSETS AND BANKRUPTCY REMOTENESS OF COVERED BONDS

Upon the insolvency of the issuer, the mortgage receivables and the related mortgage certificates and substitute assets would not form part of the issuer's estate. Accordingly, the asset cover pool may be managed and enforced by the guarantors independently from the corporate insolvency proceedings of the issuers. There are a number of trigger events for default, the first being an issuer event of default. This can occur in a number of situations including the following:

> Failure to pay any interest or principal amount when due.

> Bankruptcy proceedings being ordered by a court or authority against the issuer.

> Failure to rectify any breach of the ACT or ICT.

An issuer event of default would not accelerate payments to covered bondholders, but would allow the trustee to activate the guarantee by serving a notice to pay on the guarantor. Upon the guarantee activation, the cover pool is frozen losing its dynamic nature and no further covered bonds may be issued. The guarantor is required to meet the covered bond obligations using the cash flows generated from the cover pool.

With the exception of one outstanding series issued under the legacy Credit Suisse programme, the covered bonds have a non-discretionary soft-bullet structure, a maximal 12-months extension of the principal repayment, in order to allow the realisation of the cover pool. The repayment extension is only granted if the bondholder representative (trustee) has served a notice to pay and neither the issuer nor the guarantor have sufficient liquidity for the repayment of the covered bond series concerned. In case of Valiant Bank, the soft bullet structure may not only applied to a covered bond series after an issuer event of default but may also applied to all outstanding covered bond series after a guarantor event of default in order to reduce fire sale risk.

The second event of default is the guarantor event of default. This would arise after an issuer event of default if the guarantor failed to make any payments when due, failure of the amortisation test or bankruptcy of the guarantor. A guarantor event of default would cause the acceleration of payments to covered bondholders and their early redemption at the amount relevant to that particular covered bonds series.

IX. RISK-WEIGHTING & COMPLIANCE WITH EUROPEAN LEGISLATION

Swiss contractual-law based covered bonds have a 20% risk weighting under the standardised approach in accordance with the EU Capital Requirement Regulation (CRR) because they have not been issued by an EU credit institution. As of 1 January 2021, Swiss contractual-law based covered bonds cannot qualify for ECB repo eligibility because they are not subject to a legislative framework. Lack of legislation also means that Swiss contractual law based covered bonds are not eligible as level 1 or 2 assets under the European Commission LCR Delegated Act.

Issuers: Credit Suisse AG, Valiant Bank AG, Credit Suisse (Schweiz) AG, Crédit Agricole next bank (Suisse) SA, Cornèr Bank SA and UBS AG.

For the most up-to-date information, please consult the new ECBC Covered Bond Comparative Database webpage on the Covered Bond Label website www.coveredbondlabel.com or via the following QR code: