PREFERRED APARTMENT COMMUNITIES INC
Form 10-Q
May 11, 2015

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-Q

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x QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended March 31, 2015
OR
¨ TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the transition period from to
Commission File No. 001-34995

Preferred Apartment Communities, Inc.
(Exact name of registrant as specified in its charter)

Maryland	27-1712193
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

3284 Northside Parkway NW, Suite 150, Atlanta, GA 30327
(Address of principal executive offices) (Zip Code)
Registrant's telephone number, including area code: (770) 818-4100

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes x No ¨

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate website, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (Sec. 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes x No ¨
Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company (as defined in Rule 12b-2 of the Exchange Act).
Large accelerated filer ¨ Accelerated filer x Non-accelerated filer ¨ Smaller reporting company ¨

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes ¨ No x

The number of shares outstanding of the registrant's Common Stock, as of May 8, 2015 was 22,225,924.

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Preferred Apartment Communities, Inc.
Consolidated Balance Sheets
(Unaudited)

	March 31, 2015	December 31, 2014
Assets		
Real estate		
Land	$ 86,434,683	$79,272,457
Building and improvements	431,348,175	377,030,987
Tenant improvements	3,232,506	3,240,784
Furniture, fixtures, and equipment	50,155,356	36,864,668
Construction in progress	268,613	66,647
Gross real estate	571,439,333	496,475,543
Less: accumulated depreciation	(31,720,212)	(26,388,066)
Net real estate	539,719,121	470,087,477
Real estate loans, net of deferred fee income ($21,536,641 and $20,313,722 carried at fair value)	141,986,808	128,306,697
Real estate loans to related parties, net	30,273,403	24,924,976
Total real estate and real estate loans, net	711,979,332	623,319,150
Cash and cash equivalents	7,614,793	3,113,270
Restricted cash	4,682,937	4,707,865
Notes receivable	9,908,893	14,543,638
Note receivable and revolving line of credit from related party	15,807,114	14,153,922
Accrued interest receivable on real estate loans	8,855,896	8,038,447
Acquired intangible assets, net of amortization of $19,470,022 and $17,030,176	11,629,424	12,702,980
Deferred loan costs, net of amortization of $1,966,396 and $1,618,858	5,500,930	5,107,068
Deferred offering costs	5,981,954	6,333,763
Tenant receivables (net of allowance of $187,621 and $103,452) and other assets	6,904,984	4,390,309
Total assets	$ 788,866,257	$696,410,412
Liabilities and equity		
Liabilities		
Mortgage notes payable	$ 404,525,906	$354,418,668
Revolving line of credit	—	24,500,000
Term loan	19,000,000	—
Real estate loan participation obligation	11,314,528	7,990,798
Accounts payable and accrued expenses	5,423,293	4,941,703
Accrued interest payable	1,154,157	1,116,750
Dividends and partnership distributions payable	5,041,220	4,623,246

Acquired below market lease intangibles, net of amortization of $842,212 and $660,259	5,710,683	5,935,931
Security deposits and other liabilities	1,604,063	1,301,442
Total liabilities	453,773,850	404,828,538
Commitments and contingencies (Note 12)		
Equity		
Stockholders' equity		
Series A Redeemable Preferred Stock, $0.01 par value per share; 989,408 shares authorized; 244,812 and 193,334 shares issued; 243,887 and 192,846 shares outstanding at March 31, 2015 and December 31, 2014, respectively	2,439	1,928
Common Stock, $0.01 par value per share; 400,066,666 shares authorized; 22,131,190 and 21,403,987 shares issued and outstanding at March 31, 2015 and December 31, 2014, respectively	221,312	214,039
Additional paid in capital	345,307,073	300,576,349
Accumulated deficit	It is impossible to predict what the correlations between the Underlyings will be over the term of the Notes. The Underlyings represent different equity markets and these different equity markets may not perform similarly over the term of the Notes. Although the correlation of the Underlyings' performance may change over the term of the Notes, the Contingent Coupon Rate is determined, in part, based on the Underlyings' performance calculated using our internal models at the time when the terms of the Notes are determined. As stated earlier, a higher Contingent Coupon Rate is generally associated with lower correlation of the Underlyings, which reflects a greater potential for missed Contingent Coupons and for a loss on your investment at maturity. See “Correlation of the Underlyings” below.	

Risks Associated with Foreign Securities Markets — Because foreign companies or foreign equity securities held by the FEZ are publicly traded in the applicable foreign countries and trade in currencies other than U.S. dollars, investments in the Notes involve particular risks. For example, the foreign securities markets may be more volatile than the U.S. securities markets, and market developments may affect these markets differently from the United States or other securities markets. Direct or indirect government intervention to stabilize the securities markets outside the United States, as well as cross-shareholdings in certain companies, may affect trading prices and trading volumes in those markets. Also, the public availability of information concerning the foreign issuers may vary depending on their home jurisdiction and the reporting requirements imposed by their respective regulators. In addition, the foreign issuers may be subject to accounting, auditing and financial reporting standards and requirements that differ from those applicable to United States reporting companies.

Securities prices generally are subject to political, economic, financial and social factors that apply to the markets in which they trade and, to a lesser extent, foreign markets. Securities prices outside the United States are subject to political, economic, financial and social factors that apply in foreign countries. These factors, which could negatively affect foreign securities markets, include the possibility of changes in a foreign government's economic and fiscal policies, the possible imposition of, or changes in, currency exchange laws or other laws or restrictions applicable to foreign companies or investments in foreign equity securities and the possibility of fluctuations in the rate of exchange between currencies. Moreover, foreign economies may differ favorably or unfavorably from the United States economy in important respects such as growth of gross national product, rate of inflation, capital reinvestment, resources and self-sufficiency.

¨ An Investment in Notes Linked to the IWM Is Subject to Risks Associated in an Investment in Stocks with a Small Market Capitalization— The IWM is linked to stocks issued by companies with relatively small market capitalizations. These companies often have greater stock price volatility, lower trading volume and less liquidity than large-capitalization companies. As a result, the share price of the IWM may be more volatile than that of a market measure that does not track solely small-capitalization stocks. Stock prices of small-capitalization companies are also often more vulnerable than those of large-capitalization companies to adverse business and economic developments, and the stocks of small-capitalization companies may be thinly traded, and be less attractive to many investors if they do not pay dividends. In addition, small capitalization companies are often less well-established and less stable financially than large-capitalization companies and may depend on a small number of key personnel, making them more vulnerable to loss of those individuals. Small capitalization companies tend to have lower revenues, less diverse product lines, smaller shares of their target markets, fewer financial resources and fewer competitive strengths than large-capitalization companies. These companies may also be more susceptible to adverse developments related to their products or services.

¨Exchange Rate Risk — The share price of the FEZ will fluctuate based in large part upon its net asset value, which will in turn depend in part upon changes in the value of the euro, the currency in which the stocks held by the FEZ are traded. Accordingly, investors in the Notes will be exposed to currency exchange rate risk with respect to each of the euro and the U.S. dollar. An investor's net exposure will depend on the extent to which the euro strengthens or weakens against the U.S. dollar. If the dollar strengthens against the euro, the net asset value of the FEZ will be adversely affected and the price of the FEZ, and consequently, the market value of the Notes may decrease.

- No Assurance that the Investment View Implicit in the Notes Will Be Successful — It is impossible to predict whether and the extent to which the prices of the Underlyings will rise or fall. The closing prices of the Underlyings will be influenced by complex and interrelated political, economic, financial and other factors that affect the Underlyings. You should be willing to accept the downside risks of owning equities in general and the Underlyings in particular, and the risk of losing some or all of your initial investment.
- Lack of Liquidity — The Notes will not be listed on any securities exchange. RBCCM intends to offer to purchase the Notes in the secondary market, but is not required to do so. Even if there is a secondary market, it may not provide enough liquidity to allow you to trade or sell the Notes easily. Because other dealers are not likely to make a secondary market for the Notes, the price at which you may be able to trade your Notes is likely to depend on the price, if any, at which RBCCM is willing to buy the Notes.
- Potential Conflicts — We and our affiliates play a variety of roles in connection with the issuance of the Notes, including hedging our obligations under the Notes. In performing these duties, the economic interests of the calculation agent and other

affiliates of ours are potentially adverse to your interests as an investor in the Notes.

.. Potentially Inconsistent Research, Opinions or Recommendations by RBCCM, UBS or Their Affiliates — RBCCM, UBS or their affiliates may publish research, express opinions or provide recommendations as to the Underlyings that are inconsistent with investing in or holding the Notes, and which may be revised at any time. Any such research, opinions or recommendations could affect the value of the Underlyings, and therefore the market value of the Notes.

- Uncertain Tax Treatment — Significant aspects of the tax treatment of an investment in the Notes are uncertain. You should consult your tax adviser about your tax situation.
- Potential Royal Bank of Canada and UBS Impact on Price — Trading or transactions by Royal Bank of Canada, UBS or our respective affiliates in one or both of the Underlyings or the securities included in an Underlying's underlying index, or in futures, options, exchange-traded funds or other derivative products on the Underlyings or those securities may adversely affect the market value of the Underlyings or the closing prices of the Underlyings, and, therefore, the market value of the Notes.
- The Terms of the Notes at Issuance Were Influenced, and Their Market Value Prior to Maturity Will Be Influenced, by Many Unpredictable Factors — Many economic and market factors influenced the terms of the Notes at issuance and will affect their value prior to maturity. These factors are similar in some ways to those that could affect the value of a combination of instruments that might be used to replicate the payments on the Notes, including a combination of a bond with one or more options or other derivative instruments. For the market value of the Notes, we expect that, generally, the price of the Underlyings on any day will affect the value of the Notes

more than any other single factor. However, you should not expect the value of the Notes in the secondary market to vary in proportion to changes in the prices of the Underlyings. The value of the Notes will be affected by a number of economic and market factors that may either offset or magnify each other, including:

- the price of each Underlying;
- the actual and expected volatility of the price of each Underlying;
- the time remaining to maturity of the Notes;
- the dividend rates on the securities held by the Underlyings;
- interest and yield rates in the market generally;
- a variety of economic, financial, political, regulatory or judicial events;
- the occurrence of certain events with respect to the Underlyings that may or may not require an adjustment to the terms of the Notes; and
- our creditworthiness, including actual or anticipated downgrades in our credit ratings.

Some or all of these factors influenced the terms of the Notes at issuance and will also influence the price you will receive if you choose to sell the Notes prior to maturity. The impact of any of the factors set forth above may enhance or offset some or all of any change resulting from another factor or factors. You may have to sell the Notes at a substantial discount from the principal amount if, for example, the price of one or both of the Underlyings is at, or not sufficiently above, its Downside Threshold.

¨ The Anti-Dilution Protection for Each Underlying Is Limited — The calculation agent will make adjustments to the Initial Price, Downside Threshold and Coupon Barrier of each Underlying for certain events affecting the shares of the Underlyings. However, the calculation agent will not be required to make an adjustment in response to all events that could affect an Underlying. If an event occurs that does not require the calculation agent to make an adjustment, the value of the Notes may be materially and adversely affected.

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Hypothetical Examples

Hypothetical terms only. Actual terms may vary. See the cover page for actual offering terms.

The following examples are hypothetical and provided for illustrative purposes only. They do not purport to be representative of every possible scenario concerning increases or decreases in the price of either Underlying relative to its Initial Price. We cannot predict the Final Price of any Underlying. You should not take these examples as an indication or assurance of the expected performance of either Underlying. The numbers appearing in the examples and tables below have been rounded for ease of analysis.

The following examples and tables illustrate the Payment at Maturity or upon an automatic call per Note on a hypothetical offering of the Notes, based on the following hypothetical assumptions (the actual Initial Prices, Coupon Barriers and Downside Thresholds are set forth on the cover page of this pricing supplement):

Principal Amount:	$10.00
Term:	Approximately three years
Hypothetical Initial Price*:	$100.00
Coupon Rate:	7.10% per annum (or 1.775% per quarter)
Coupon**:	$0.1775 per quarter
	Quarterly

Coupon Observation Dates:	
Call Observation Dates:	Quarterly (callable after six months)
Hypothetical Initial Prices*:	
Underlying A:	$100.00
Underlying B:	$100.00
Hypothetical Coupon Barriers*:	
Underlying A:	$70.00 (which is 70% of its Initial Price)
Underlying B:	$70.00 (which is 70% of its Initial Price)
Hypothetical Downside Thresholds*:	
Underlying A:	$70.00 (which is 70% of its Initial Price)
Underlying B:	$70.00 (which is 70% of its Initial Price)

* Not the actual Initial Price, Coupon Barrier or Downside Threshold applicable to the Notes. The actual Initial Price, Coupon Barrier and Downside Threshold are set forth on the cover page of this pricing supplement.
** Contingent Coupon payments, if payable, will be paid in arrears in equal quarterly installments during the term of the Notes unless earlier called.

Scenario #1: Notes Are Called on the Fourth Coupon Observation Date.

Date	Closing Price	Payment (per Note)
First Coupon Observation Date	Underlying A: $100.00 (at or above Initial Price)	$0.1775 (Contingent Coupon – not callable)
	Underlying B: $110.00 (at or above Initial Price)	
Second Coupon Observation Date	Underlying A: $95.00 (at or above Coupon Barrier; below Initial Price)	$0.00 (Notes are not called)
	Underlying B: $60.00 (below Coupon Barrier)	
Third Coupon Observation Date	Underlying A: $95.00 (at or above Coupon Barrier; below Initial Price)	$0.00 (Notes are not called)
	Underlying B: $60.00 (below Coupon Barrier)	

Fourth Coupon Observation Date	Underlying A: $110.00 (at or above Initial Price)	$10.1775 (settlement amount)
	Underlying B: $115.00 (at or above Initial Price)	
	Total Payment:	$10.355 (3.55% return)

Since the Notes are called on the fourth Coupon Observation Date, we will pay you on the Call Settlement Date a total of $10.1775 per Note, reflecting your principal amount plus the applicable Contingent Coupon. When added to the Contingent Coupon payments of $0.1775 received in respect of a prior Coupon Observation Date, we will have paid you a total of $10.355 per Note, for a 3.55% total return on the Notes. No further amount will be owed to you under the Notes.

Scenario #2: Notes Are NOT Called and the Final Prices of Both Underlyings Are at or Above Their Respective Downside Thresholds.

Date	Closing Price	Payment (per Note)
First Coupon Observation Date	Underlying A: $110.00 (at or above Coupon Barrier; below Initial Price)	$0.1775 (Contingent Coupon – not callable)
	Underlying B: $80.00 (at or above Coupon Barrier; below Initial Price)	
Second Coupon Observation Date	Underlying A: $50.00 (below Coupon Barrier)	$0.00 (Notes are not called)
	Underlying B: $90.00 (at or above Coupon Barrier; below Initial Price)	
Third Coupon Observation Date	Underlying A: $95.00 (at or above Coupon Barrier; below Initial Price)	$0.00 (Notes are not called)

	Underlying B: $40.00 (below Coupon Barrier)	
Fourth Coupon Observation Date	Underlying A: $95.00 (at or above Coupon Barrier; below Initial Price)	$0.00 (Notes are not called)
	Underlying B: $60.00 (below Coupon Barrier)	
Fifth through Eleventh Coupon Observation Dates	Underlying A: Various (below Coupon Barrier) Underlying B: Various (above Initial Price)	$0.00 (Notes are not called)
Final Valuation Date	Underlying A: $90.00 (at or above Downside Threshold and Coupon Barrier; below Initial Price)	$10.1775 (Payment at Maturity)
	Underlying B: $115.00 (at or above Downside Threshold, Coupon Barrier and	

	Initial Price)	
	Total Payment:	$10.355 (3.55% return)

At maturity, we will pay you a total of $10.1775 per Note, reflecting your principal amount plus the applicable Contingent Coupon. When added to the Contingent Coupon payment of $0.1775 received in respect of a prior Coupon Observation Date, we will have paid you a total of $10.335 per Note, for a 3.55% total return on the Notes.

Scenario #3: Notes Are NOT Called and the Final Price of One Underlying Is Below its Downside Threshold

Date	Closing Price	Payment (per Note)
First Coupon Observation Date	Underlying A: $85.00 (at or above Coupon Barrier; below Initial Price)	$0.1775 (Contingent Coupon – not callable)
	Underlying B: $120.00 (above Initial Price)	
Second Coupon Observation Date	Underlying A: $90.00 (at or above Coupon Barrier; below Initial Price)	$0.1775 (Contingent Coupon – not called)
	Underlying B: $80.00	

	(at or above Coupon Barrier; below Initial Price)	
Third Coupon Observation Date	Underlying A: $220.00 (above Initial Price) Underlying B: $80.00 (at or above Coupon Barrier; below Initial Price)	$0.1775 (Contingent Coupon – not called)
Fourth Coupon Observation Date	Underlying A: $95.00 (at or above Coupon Barrier; below Initial Price) Underlying B: $60.00 (below Coupon Barrier)	$0.00 (Notes are not called)
Fifth through Eleventh Coupon Observation Dates	Underlying A: Various (below Coupon Barrier) Underlying B: Various (above Initial Price)	$0.00 (Notes are not called)
Final Valuation Date	Underlying A: $50.00 (below	$10.00 + [$10.00 × Underlying

Downside Threshold and Coupon Barrier) Underlying B: $130.00 (above Initial Price)	Return] = $10.00 + [$10.00 × -50%] = $10.00 - $5.00 = $5.00 (Payment at Maturity)
Total Payment:	$5.5325 (-44.675% return)

Since the Notes are not called and the Final Price of the Least Performing Underlying is below the Downside Threshold, we will pay you at maturity $5.00 per Note. When added to the Contingent Coupon payments of $0.5325 received in respect of prior Coupon Observation Dates, we will have paid you $5.5325 per Note, for a loss on the Notes of 44.675%.

The Notes differ from ordinary debt securities in that, among other features, we are not necessarily obligated to repay the full amount of your initial investment. If the Notes are not called on any Call Observation Date, you may lose some or all of your initial investment. Specifically, if the Notes are not called and the Final Price of one or both of the Underlyings is less than its Downside Threshold, you will lose 1% (or a fraction thereof) of your principal amount for each 1% (or a fraction thereof) that the Underlying Return of the Least Performing Underlying is less than zero. Any payment on the Notes, including payments in respect of an automatic call, Contingent Coupon or any repayment of principal provided at maturity, is dependent on our ability to satisfy our obligations when they come due. If we are unable to meet our obligations, you may not receive any amounts due to you under the Notes.

What Are the Tax Consequences of the Notes?

U.S. Federal Income Tax Consequences

The following, together with the discussion of U.S. federal income tax in the accompanying product prospectus supplement, prospectus supplement, and prospectus, is a general description of the material U.S. federal income tax consequences relating to an investment in the Notes. The following summary is not complete and is qualified in its entirety by the discussion under the section entitled "Supplemental Discussion of U.S. Federal Income Tax Consequences" in the accompanying product prospectus supplement no. UBS-TPAOS-2, the section entitled "Certain Income Tax Consequences" in the accompanying prospectus supplement, and the section entitled "Tax Consequences" in the accompanying prospectus, which you should carefully review prior to investing in the Notes.

In the opinion of our counsel, Morrison & Foerster LLP, it would generally be reasonable to treat the Notes as a callable pre-paid cash-settled contingent income-bearing derivative contract linked to the Underlying for U.S. federal income tax purposes, and the terms of the Notes require a holder and us (in the absence of a change in law or an administrative or judicial ruling to the contrary) to treat the Notes for all tax purposes in accordance with such characterization. Although the U.S. federal income tax treatment of the Contingent Coupons is uncertain, we intend to take the position, and the following discussion assumes, that such Contingent Coupons (including any coupon paid on or with respect to the call or maturity date) constitute taxable ordinary income to a U.S. holder at the time received or accrued in accordance with the holder's regular method of accounting. If the Notes are treated as described above, subject to the potential application of the "constructive ownership" rules under Section 1260 of the Internal Revenue Code, a U.S. holder should generally recognize capital gain or loss upon the call, sale or maturity of the Notes in an amount equal to the difference between the amount a holder receives at such time (other than amounts properly attributable to any Contingent Coupon, which would be taxed, as described above, as ordinary income) and the holder's tax basis in the Notes. Capital gain recognized by an individual U.S. holder is generally taxed at preferential rates where the property is held for more than one year and is generally taxed at ordinary income rates where the property is held for one year or less. The deductibility of capital losses is subject to limitations.

Alternative tax treatments are also possible and the Internal Revenue Service might assert that a treatment other than that described above is more appropriate. In addition, the

Internal Revenue Service has released a notice that may affect the taxation of holders of the Notes. According to the notice, the Internal Revenue Service and the Treasury Department are actively considering whether the holder of an instrument such as the Notes should be required to accrue ordinary income on a current basis. It is not possible to determine what guidance they will ultimately issue, if any. It is possible, however, that under such guidance, holders of the Notes will ultimately be required to accrue income currently and this could be applied on a retroactive basis. The Internal Revenue Service and the Treasury Department are also considering other relevant issues, including whether additional gain or loss from such instruments should be treated as ordinary or capital and whether the special "constructive ownership rules" of Section 1260 of the Internal Revenue Code might be applied to such instruments. Holders are urged to consult their tax advisors concerning the significance, and the potential impact, of the above considerations.

Individual holders that own “specified foreign financial assets” may be required to include certain information with respect to such assets with their U.S. federal income tax return. You are urged to consult your own tax advisor regarding such requirements with respect to the Notes.

Under Section 871(m) of the Internal Revenue Code, a “dividend equivalent” payment is treated as a dividend from sources within the United States. Such payments generally would be subject to a 30% U.S. withholding tax if paid to a non-U.S. holder. Under U.S. Treasury Department regulations, payments (including deemed payments) with respect to equity-linked instruments ("ELIs") that are "specified ELIs" may be treated as dividend equivalents if such specified ELIs reference an interest in an "underlying security," which is generally any interest in an entity taxable as a corporation for U.S. federal income tax purposes if a payment with respect to such interest could give rise to a U.S. source dividend. However, the IRS has issued guidance that states that the U.S. Treasury Department and the IRS intend to amend the effective dates of the U.S. Treasury Department regulations to provide that withholding on dividend equivalent payments will not apply to specified ELIs that are not delta-one instruments and that are issued before January 1, 2019. Based on our determination that the Notes are not delta-one instruments, non-U.S. holders should not be subject to withholding on dividend equivalent payments, if any, under the Notes. However, it is possible that the Notes could be treated as deemed reissued for U.S. federal income tax purposes upon the occurrence of certain events affecting the Underlying or the Notes, and following such occurrence the Notes could be treated as subject to withholding on dividend equivalent payments.

Non-U.S. holders that enter, or have entered, into other transactions in respect of the Underlying or the Notes should consult their tax advisors as to the application of the dividend equivalent withholding tax in the context of the Notes and their other transactions. If any payments are treated as dividend equivalents subject to withholding, we (or the applicable withholding agent) would be entitled to withhold taxes without being required to pay any additional amounts with respect to amounts so withheld.

The Notes are not intended for purchase by any investor that is not a United States person, as that term is defined for U.S. federal income tax purposes, and the underwriters will not make offers of the Notes to any such investor.

Canadian Federal Income Tax Consequences

For a discussion of the material Canadian federal income tax consequences relating to an investment in the Notes, please see the section entitled "Tax Consequences—Canadian Taxation" in the accompanying prospectus, which you should carefully review prior to investing in the Notes.

Information About the Underlyings

We have derived the following information regarding each of the applicable Underlyings from publicly available documents. We have not independently verified the accuracy or completeness of the following information. We are not affiliated with any of the Underlyings and the Underlyings will have no obligations with respect to the Notes. This document relates only to the Notes and does not relate to the shares of any of the Underlying or any securities included in any of the underlying indices of the Underlyings. Neither we nor any of our affiliates participates in the preparation of the publicly available documents described below. Neither we nor any of our affiliates has made any due diligence inquiry with respect to any of the Underlyings in connection with the offering of any of the Notes. There can be no assurance that all events occurring prior to the date of this document, including events that would affect the accuracy or completeness of the publicly available documents described below, that would affect the trading prices of the shares of any of the Underlyings have been or will be publicly disclosed. Subsequent disclosure of any events or the disclosure of or failure to disclose material future events concerning any of the Underlyings could affect the price of the shares of the applicable Underlying after the trade date, and therefore could affect the payment at maturity.

The selection of the Underlyings relating to the Notes is not a recommendation to buy or sell the shares of any of the Underlyings. Neither we nor any of our affiliates make any representation to you as to the performance of the shares of any of the Underlyings.

Information provided to or filed with the SEC under the Securities Exchange Act of 1934 and the Investment Company Act of 1940 relating to each Underlying may be obtained through the SEC's website at http://www.sec.gov.

The iShares® Russell 2000 ETF

iShares consists of separate investment portfolios (the "iShares Funds"), including the IWM. The IWM seeks investment results that correspond generally to the price and yield performance, before fees and expenses, of its underlying index. The IWM typically earns income from dividends from securities it holds. These amounts, net of expenses and taxes (if applicable), are passed along to shareholders of the IWM as "ordinary income." In addition, the IWM realizes capital gains or losses whenever they sell securities. Net long-term capital gains are distributed to the IWMs shareholders as "capital gain distributions." However, because the Notes are linked to the share price of the IWM, you will not be entitled to receive income, dividend, or capital gain distributions from the applicable Underlying or any equivalent payments. "iShares®" and "BlackRock®" are registered trademarks of BlackRock®. The Notes are not sponsored, endorsed, sold, or promoted by BlackRock®, or by any of the iShares® funds. Neither BlackRock® nor the iShares® funds make any representations or warranties to the owners of any of the Notes or any member of the public regarding the advisability of investing in any of the Notes. Neither BlackRock® nor the iShares® funds shall have any obligation or liability in connection with the registration, operation, marketing, trading, or sale of any of the Notes or in connection with our use of information about any of the IWM or any of the iShares® funds.

The IWM seeks investment results that correspond generally to the price and yield performance, before fees and expenses, of the Russell 2000® Index. The shares of this underlying trade on the NYSE Arca, Inc. under the symbol "IWM."

Russell 2000® Index

The Russell 2000® Index (Bloomberg L.P. index symbol "RTY") was developed by Russell Investments ("Russell") before FTSE International Limited ("FTSE") and Russell combined in 2015 to create FTSE Russell, which is wholly owned by London Stock Exchange Group. Russell began dissemination of the RTY on January 1, 1984. FTSE Russell calculates and publishes the RTY. The

RTY was set to 135 as of the close of business on December 31, 1986. The RTY is designed to track the performance of the small capitalization segment of the U.S. equity market. As a subset of the Russell 3000® Index, the RTY consists of the smallest 2,000 companies included in the Russell 3000® Index. The Russell 3000® Index measures the performance of the largest 3,000 U.S. companies, representing approximately 98% of the investable U.S. equity market. The RTY is determined, comprised, and calculated by FTSE Russell without regard to the Notes.

Selection of Stocks Comprising the RTY

All companies eligible for inclusion in the RTY must be classified as a U.S. company under the index sponsor’s country-assignment methodology. If a company is incorporated, has a stated headquarters location, and trades in the same country (American Depositary Receipts and American Depositary Shares are not eligible), then the company is assigned to its country of incorporation. If any of the three factors are not the same, the index sponsor defines three Home Country Indicators (“HCIs”): country of incorporation, country of headquarters, and country of the most liquid exchange (as defined by a two-year average daily dollar trading volume) (“ADDTV”) from all exchanges within a country. Using the HCIs, the index sponsor compares the primary location of the company's assets with the three HCIs. If the primary location of its assets matches any of the HCIs, then the company is assigned to the primary location of its assets. If there is insufficient information to determine the country in which the company's assets are primarily located, the index sponsor will use the primary country from which the company's revenues are primarily derived for the comparison with the three HCIs in a similar manner. The index sponsor uses the average of two years of assets or revenues data to reduce potential turnover. If conclusive country details cannot be derived from assets or revenues data, the index sponsor will assign the company to the country of its headquarters, which is defined as the address of the company's principal executive offices, unless that country is a Benefit Driven Incorporation "BDI" country, in which case the company will be assigned to the country of its most liquid stock exchange. BDI countries include: Anguilla, Antigua and Barbuda, Aruba, Bahamas, Barbados, Belize, Bermuda, Bonaire, British Virgin Islands, Cayman Islands, Channel Islands, Cook Islands, Curacao, Faroe Islands, Gibraltar, Guernsey, Isle of Man, Jersey, Liberia, Marshall Islands, Panama, Saba, Sint Eustatius, Sint Maarten, and Turks and Caicos Islands. For any companies incorporated or headquartered in a U.S. territory, including countries such as Puerto Rico, Guam,

and U.S. Virgin Islands, a U.S. HCI is assigned.
All securities eligible for inclusion in the RTY must trade on a major U.S. exchange. Stocks must have a closing price at or above $1.00 on their primary exchange on the last trading day in May to be eligible for inclusion during annual reconstitution. However, in order to reduce unnecessary turnover, if an existing member's closing price is less than $1.00 on the last day of May, it will be considered eligible if the average of the daily closing prices (from its primary exchange) during the month of May is equal to or greater than $1.00. Initial public offerings are added each quarter and must have a closing price at or above $1.00 on the last day of their eligibility period in order to qualify for index inclusion. If an existing stock does not trade on the "rank day" (typically the last trading day in May, but a confirmed timetable is announced each spring), but does have a closing price at or above $1.00 on another eligible U.S. exchange, that stock will be eligible for inclusion.
An important criterion used to determine the list of securities eligible for the RTY is total market capitalization, which is defined as the market price as of the rank day in May for those securities being considered at annual reconstitution times the total number of shares outstanding. Where applicable, common stock, non-restricted exchangeable shares and partnership units/membership

interests are used to determine market capitalization. Any other form of shares such as preferred stock, convertible preferred stock, redeemable shares, participating preferred stock, warrants, rights, installment receipts or trust receipts, are excluded from the calculation. If multiple share classes of common stock exist, they are combined to determine total shares outstanding. In cases where the common stock share classes act independently of each other (e.g., tracking stocks), each class is considered for inclusion separately. If multiple share classes exist, the pricing vehicle will be designated as the share class with the highest two-year trading volume as of the rank day in May.

Companies with a total market capitalization of less than $30 million are not eligible for the RTY. Similarly, companies with only 5% or less of their shares available in the marketplace are not eligible for the RTY. Royalty trusts, limited liability companies, closed-end investment companies (companies that are required to report Acquired Fund Fees and Expenses, as defined by the SEC, including business development companies), blank check companies, special purpose acquisition companies, and limited partnerships are also ineligible for inclusion. Exchange traded funds and mutual funds are also excluded. Bulletin board, pink-sheets and over-the-counter ("OTC") traded securities are not eligible for inclusion.

Annual reconstitution is a process by which the RTY is completely rebuilt. Based on closing levels of the company's common stock on its primary exchange on the rank day of May of each year, FTSE Russell reconstitutes the composition of the RTY using the then existing market capitalizations of eligible companies. Reconstitution of the RTY occurs on the last Friday in June or, when the last Friday in June is the 29th or 30th, reconstitution occurs on the prior Friday. In addition, the index sponsor adds initial public offerings to the RTY on a quarterly basis based on total market capitalization ranking within the market-adjusted capitalization breaks established during the most recent reconstitution.

After membership is determined, a security’s shares are adjusted to include only those shares available to the public. This is often referred to as “free float.” The purpose of the adjustment is to exclude from market calculations the capitalization that is not available for purchase and is not part of the investable opportunity set.

Historical Information

The following table sets forth the quarterly high, low and period-end closing prices of the IWM, as reported by Bloomberg Financial Markets. The historical performance of the IWM should not be taken as an indication of its future performance. We cannot give you assurance that the performance of the IWM will result in the return of any of your initial investment.

Quarter Begin	Quarter End	Quarterly Closing High	Quarterly Closing Low	Quarterly Period-End Close
1/1/2008	3/31/2008	$75.12	$64.30	$68.51
4/1/2008	6/30/2008	$76.17	$68.47	$69.03
7/1/2008	9/30/2008	$75.20	$65.50	$68.39
10/1/2008	12/31/2008	$67.02	$38.58	$49.27
1/1/2009	3/31/2009	$51.27	$34.36	$41.94
4/1/2009	6/30/2009	$53.19	$42.82	$50.96
7/1/2009	9/30/2009	$62.02	$47.87	$60.23
10/1/2009	12/31/2009	$63.36	$56.22	$62.26
1/1/2010	3/31/2010	$69.25	$58.68	$67.81
4/1/2010	6/30/2010	$74.14	$61.08	$61.08
7/1/2010	9/30/2010	$67.67	$59.04	$67.47
10/1/2010	12/31/2010	$79.22	$66.94	$78.23
1/1/2011	3/31/2011	$84.17	$77.18	$84.17
4/1/2011	6/30/2011	$86.37	$77.77	$82.80
7/1/2011	9/30/2011	$85.65	$64.25	$64.25
10/1/2011	12/31/2011	$76.45	$60.97	$73.69
1/1/2012	3/31/2012	$84.41	$74.56	$82.85
4/1/2012	6/30/2012	$83.79	$73.64	$79.65
7/1/2012	9/30/2012	$86.40	$76.68	$83.46
10/1/2012	12/31/2012	$84.69	$76.88	$84.29
1/1/2013	3/31/2013	$94.80	$86.65	$94.26
4/1/2013	6/30/2013	$99.51	$89.58	$97.16
7/1/2013	9/30/2013	$107.10	$98.08	$106.62
10/1/2013	12/31/2013	$115.31	$103.67	$115.31
1/1/2014	3/31/2014	$119.83	$108.64	$116.34
4/1/2014	6/30/2014	$118.81	$108.88	$118.81
7/1/2014	9/30/2014	$120.02	$109.35	$109.35
10/1/2014	12/31/2014	$121.08	$104.30	$119.67
1/1/2015	3/31/2015	$126.03	$114.69	$124.35
4/1/2015	6/30/2015	$129.01	$120.85	$124.86
7/1/2015	9/30/2015	$126.31	$107.53	$109.20
10/1/2015	12/31/2015	$119.85	$109.01	$112.51
1/1/2016	3/31/2016	$110.62	$94.80	$110.62
4/1/2016	6/30/2016	$118.43	$108.69	$114.97

7/1/2016	9/30/2016	$125.70	$113.69	$124.21
10/1/2016	12/31/2016	$138.31	$115.00	$134.85
1/1/2017	3/31/2017	$140.36	$133.75	$137.48
4/1/2017	6/30/2017	$142.10	$133.72	$140.92
7/1/2017	9/30/2017	$148.18	$134.83	$148.18
10/1/2017	11/7/2017*	$150.33	$147.00	$147.00

* This pricing supplement includes information for the fourth calendar quarter of 2017 for the period from October 1, 2017 through November 7, 2017. Accordingly, the “Quarterly Closing High,” “Quarterly Closing Low” and “Quarterly Period-End Close” data indicated are for this shortened period only and do not reflect complete data for the fourth calendar quarter of 2017.

The graph below illustrates the performance of the IWM from January 2, 2008 to November 7, 2017, based on its Initial Price of $147.00, which was its closing price on November 7, 2017. The solid line represents its Downside Threshold and Coupon Barrier of $102.90, which is equal to 70% of its Initial Price on November 7, 2017.

n Coupon Barrier / Downside Threshold = 70.00%

HISTORIC PERFORMANCE IS NOT AN INDICATION OF FUTURE PERFORMANCE.

Source: Bloomberg L.P. We have not independently verified the accuracy or completeness of the information obtained from Bloomberg Financial Markets.

The SPDR® EURO STOXX 50® ETF

The FEZ is an investment portfolio maintained and managed by SSFM. SSFM is the investment advisor to each of ten separate investment portfolios, including the FEZ, all of which are offered by the SPDR® Series Trust, a registered investment company. The SPDR® EURO STOXX 50® ETF trades on the NYSE Arca under the ticker symbol "FEZ." Information provided to or filed with the SEC by the SPDR® Series Trust under the Securities Exchange Act of 1934 can be located by reference to its Central Index Key, or CIK, 1064642 through the SEC's website at http://www.sec.gov. Additional information about SSFM and the FEZ may be obtained from other sources including, but not limited to, press releases, newspaper articles and other publicly disseminated documents. We make no representation or warranty as to the accuracy or completeness of such information.

Each Underlying Asset seeks to provide investment results that, before fees and expenses, correspond generally to the total return performance of the EURO STOXX 50® Index (the "SX5E" or the "Underlying Index"). The FEZ utilizes a "replication" investment approach in attempting to track the performance of the Underlying Index. The FEZ typically invests in substantially all of the securities which comprise the Underlying Index in approximately the same proportions as the Underlying Index. The FEZ will normally invest at least 80% of its total assets in common stocks that comprise the Underlying Index.

The EURO STOXX 50® Index

The SX5E was created by STOXX Limited, a subsidiary of Deutsche Börse AG. Publication of the SX5E began in February 1998, based on an initial SX5E level of 1,000 at December 31, 1991.

Composition and Maintenance

The SX5E is composed of 50 component stocks of market sector leaders from within the 19 EURO STOXX® Supersector indices, which represent the Eurozone portion of the STOXX Europe 600® Supersector indices.

The composition of the SX5E is reviewed annually, based on the closing stock data on the last trading day in August. The component stocks are announced on the first trading day in September. Changes to the component stocks are implemented on the third Friday in September and are effective the following trading day. Changes in the composition of the SX5E are made to ensure that the SX5E includes the 50 market sector leaders from within the SX5E.

The free float factors for each component stock used to calculate the SX5E, as described below, are reviewed, calculated, and implemented on a quarterly basis and are fixed until the next quarterly review.

The SX5E is also reviewed on an ongoing monthly basis.

Corporate actions (including initial public offerings, mergers and takeovers, spin-offs, delistings, and bankruptcy) that affect the SX5E composition are announced immediately, implemented two trading days later and become effective on the next trading day after implementation.

Calculation of the SX5E

The SX5E is calculated with the "Laspeyres formula," which measures the aggregate price changes in the component stocks against a fixed base quantity weight. The formula for calculating the SX5E value can be expressed as follows:

$$\text{Index} = \frac{\text{Free float market capitalization of the SX5E}}{\text{Divisor}} \times 1{,}000$$

The "free float market capitalization of the SX5E" is equal to the sum of the products of the price, the number of shares, the free float factor and the weighting cap factor for each component stock as of the time the SX5E is being calculated.

The SX5E is also subject to a divisor, which is adjusted to maintain the continuity of the SX5E values across changes due to corporate actions, such as the deletion and addition of stocks, the substitution of stocks, stock dividends, and stock splits.

Historical Information

The following table sets forth the quarterly high, low and period-end closing prices of the FEZ, as reported by Bloomberg Financial Markets. The historical performance of the FEZ should not be taken as an indication of its future performance. We cannot give you assurance that the performance of the FEZ will result in the return of any of your initial investment.

Quarter Begin	Quarter End	Quarterly Closing High	Quarterly Closing Low	Quarterly Period-End Close
1/1/2008	3/31/2008	$62.76	$52.71	$56.35
4/1/2008	6/30/2008	$60.36	$51.31	$51.31
7/1/2008	9/30/2008	$52.22	$41.13	$42.59
10/1/2008	12/31/2008	$42.55	$26.35	$34.35
1/1/2009	3/31/2009	$34.93	$22.28	$27.15
4/1/2009	6/30/2009	$36.63	$27.68	$33.30
7/1/2009	9/30/2009	$42.18	$31.35	$41.33
10/1/2009	12/31/2009	$43.55	$39.58	$41.48
1/1/2010	3/31/2010	$43.10	$35.37	$38.90
4/1/2010	6/30/2010	$40.55	$30.01	$30.57
7/1/2010	9/30/2010	$37.16	$30.87	$36.71
10/1/2010	12/31/2010	$40.47	$34.04	$36.84
1/1/2011	3/31/2011	$41.34	$35.28	$40.71
4/1/2011	6/30/2011	$44.03	$37.61	$40.60
7/1/2011	9/30/2011	$41.18	$26.49	$28.28
10/1/2011	12/31/2011	$34.92	$27.24	$29.51
1/1/2012	3/31/2012	$33.92	$28.59	$32.46
4/1/2012	6/30/2012	$32.76	$25.83	$28.22
7/1/2012	9/30/2012	$33.41	$25.47	$31.03
10/1/2012	12/31/2012	$34.79	$30.54	$34.66
1/1/2013	3/31/2013	$36.40	$32.78	$33.04
4/1/2013	6/30/2013	$36.58	$32.44	$33.11
7/1/2013	9/30/2013	$39.13	$32.80	$38.38
10/1/2013	12/31/2013	$42.20	$38.48	$42.20
1/1/2014	3/31/2014	$42.66	$38.94	$42.66
4/1/2014	6/30/2014	$45.11	$42.16	$43.27
7/1/2014	9/30/2014	$43.81	$39.26	$39.70
10/1/2014	12/31/2014	$39.70	$35.94	$36.86
1/1/2015	3/31/2015	$39.67	$34.86	$38.82
4/1/2015	6/30/2015	$40.71	$37.43	$37.43
7/1/2015	9/30/2015	$39.59	$33.18	$33.85
10/1/2015	12/31/2015	$37.05	$33.74	$34.43
1/1/2016	3/31/2016	$33.70	$29.92	$33.23
4/1/2016	6/30/2016	$34.75	$29.18	$31.15

7/1/2016	9/30/2016	$33.81	$29.88	$32.76
10/1/2016	12/31/2016	$33.46	$31.08	$33.46
1/1/2017	3/31/2017	$36.54	$33.53	$36.35
4/1/2017	6/30/2017	$40.18	$35.55	$38.47
7/1/2017	9/30/2017	$41.25	$38.39	$41.25
10/1/2017	11/7/2017*	$41.89	$41.05	$41.25

* This pricing supplement includes information for the fourth calendar quarter of 2017 for the period from October 1, 2017 through November 7, 2017. Accordingly, the “Quarterly Closing High,” “Quarterly Closing Low” and “Quarterly Period-End Close” data indicated are for this shortened period only and do not reflect complete data for the fourth calendar quarter of 2017.

The graph below illustrates the performance of the FEZ from January 2, 2008 to November 7, 2017, based on its Initial Price of $41.25, which was its closing price on November 7, 2017. The solid line represents its Downside Threshold and Coupon Barrier of $28.88 (rounded to two decimal places), which is equal to 70% of its Initial Price on November 7, 2017.

n Coupon Barrier / Downside Threshold = 70.00%

HISTORIC PERFORMANCE IS NOT AN INDICATION OF FUTURE PERFORMANCE.

Source: Bloomberg L.P. We have not independently verified the accuracy or completeness of the information obtained from Bloomberg Financial Markets.

Correlation of the Underlyings

The graph below illustrates the daily performance of the Underlyings from January 2, 2008 through November 7, 2017. For comparison purposes, each Underlying has been normalized to have a closing price of $100.00 on January 2, 2008 by dividing the closing price of that Underlying on each day by the closing price of that Underlying on January 2, 2008 and multiplying by $100.00. We obtained the closing prices used to determine the normalized closing prices set forth below from Bloomberg L.P., without independent verification. Past performance of the Underlyings is not indicative of their future performance.

The correlation of a pair of Underlyings represents a statistical measurement of the degree to which the returns of those Underlyings were similar to each other over a given period in terms of timing and direction (i.e., positive or negative). The closer the relationship of the daily returns of the Underlyings over a given period, the more positively correlated those Underlyings are. The graph above illustrates the historical performance of the Underlyings relative to one another over the time period shown and provides an indication of how close the relative performance of the daily returns of one

Underlying has historically been to the other. The lower (or more negative) the correlation between two Underlyings, the less likely it is that those Underlyings will move in the same direction and, therefore, the greater the potential for one of those Underlyings to close below its Coupon Barrier or Downside Threshold on any Coupon Observation Date or the Final Valuation Date, respectively. This is because the less positively correlated a pair of Underlyings are, the greater the likelihood that at least one of those Underlyings will decrease in value. This results in a greater potential for a Contingent Coupon not to be paid during the term of the Notes and for a loss of principal at maturity. However, even if the two Underlyings have a higher positive correlation, one or both of those Underlyings might close below its Coupon Barrier or Downside Threshold on a Coupon Observation Date or the Final Valuation Date, as both of those Underlyings may decrease in value together. The lower the correlation between two Underlyings, the greater the potential for one of those Underlyings to close below its Coupon Barrier or its Downside Threshold on any Coupon Observation Date or the Final Valuation Date, respectively. Therefore, the greater the number of Underlyings, the greater the potential for missed Contingent Coupons and for a loss of principal at maturity. We determine the Contingent

Coupons for the Notes based, in part, on the correlation among the Underlyings, calculated using internal models at the time the terms of the Notes are set. As discussed above, increased risk resulting from lower correlation or from a greater number of Underlyings will be reflected in a higher Contingent Coupon than would be payable on securities linked to fewer Underlyings or that have a higher degree of correlation.

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Supplemental Plan of Distribution (Conflicts of Interest)

We have agreed to indemnify UBS and RBCCM against liabilities under the Securities Act of 1933, as amended, or to contribute payments that UBS and RBCCM may be required to make relating to these liabilities as described in the prospectus supplement and the prospectus. We have agreed that UBS Financial Services Inc. may sell all or a part of the Notes that it will purchase from us to investors at the price to public or to its affiliates at the price indicated on the cover of this pricing supplement.

Subject to regulatory constraints and market conditions, RBCCM intends to offer to purchase the Notes in the secondary market, but it is not required to do so.

We or our affiliates may enter into swap agreements or related hedge transactions with one of our other affiliates or unaffiliated counterparties in connection with the sale of the Notes and RBCCM and/or an affiliate may earn additional income as a result of payments pursuant to the swap or related hedge transactions. See “Use of Proceeds and Hedging” in the accompanying product prospectus supplement no. UBS-TPAOS-2.

We expect to deliver the Notes on a date that is greater than two business days following the trade date. Under Rule 15c6-1 of the Exchange Act, trades in the secondary market generally are required to settle in two business days, unless the parties to any such trade expressly agree otherwise. Accordingly, purchasers who wish to trade the Notes more than two business days prior to the original issue date will be required to specify alternative settlement arrangements to prevent a failed settlement.

The value of the Notes shown on your account statement may be based on RBCCM's estimate of the value of the Notes if RBCCM or another of our affiliates were to make a market in the Notes (which it is not obligated to do). That estimate will be based upon the price that RBCCM may pay for the Notes in light of then prevailing market conditions, our creditworthiness and transaction costs. For a period of approximately eight months after the issue date of the Notes, the value of the Notes that may be shown on your account statement may be higher than RBCCM's estimated value of the Notes at that time. This is because the estimated value of the Notes will not include the underwriting discount and our hedging costs and profits; however, the value of the Notes shown on your account statement during that period may be a higher amount, reflecting the addition of the underwriting discount and our estimated costs and profits from hedging the Notes. Any such excess is expected to decrease over time until the end of this period. After this period, if RBCCM repurchases your Notes, it expects to do so at prices that reflect their estimated value. This period may be reduced at RBCCM's discretion based on a variety of factors, including but not limited to, the amount of the Notes that we repurchase and our negotiated arrangements from time to time with UBS.

For additional information as to the relationship between us and RBCCM, please see the section "Plan of Distribution—Conflicts of Interest" in the prospectus dated January 8, 2016.

Structuring the Notes

The Notes are our debt securities, the return on which is linked to the performance of the Underlying. As is the case for all of our debt securities, including our structured notes, the economic terms of the Notes reflect our actual or perceived creditworthiness at the time of pricing. In addition, because structured notes result in increased operational, funding and liability management costs to us, we typically borrow the funds under these Notes at a rate that is more favorable to us than the rate that we might pay for a conventional fixed or floating rate debt security of comparable maturity. Using this relatively lower implied borrowing rate rather than the secondary market rate is a factor that resulted in a higher initial estimated value of the Notes at the time their terms are set than if the secondary market rate was used. Unlike the estimated value included on the cover of this document, any value of the Notes determined for purposes of a secondary market transaction may be based on a different borrowing rate, which may result in a lower value for the Notes than if our initial internal borrowing rate were used.

In order to satisfy our payment obligations under the Notes, we may choose to enter into certain hedging arrangements (which may include call options, put options or other derivatives) on the issue date with RBCCM or one of our other subsidiaries. The terms of these hedging arrangements take into account a number of factors, including our creditworthiness, interest rate movements, the volatility of each Underlying, and the tenor of the Notes. The economic terms of the Notes and their initial estimated value depend in part on the terms of these hedging arrangements.

The lower implied borrowing rate is a factor that reduces the economic terms of the Notes to you. The initial offering price of the Notes also reflects the underwriting commission and our estimated hedging costs. These factors resulted in the initial estimated value for the Notes on the trade date being less than their public offering price. See “Key Risks—The Initial Estimated Value of the Notes Is Less than the Price to the Public” above.

Terms Incorporated in Master Note

The terms appearing above under the caption “Final Terms of the Notes” and the provisions in the accompanying product prospectus supplement no. UBS-TPAOS-2 dated January 20, 2016 under the caption “General Terms of the Securities” are incorporated into the master note issued to DTC, the registered holder of the Notes.

Validity of the Notes

In the opinion of Norton Rose Fulbright Canada LLP, the issue and sale of the Notes has been duly authorized by all necessary corporate action of the Bank in conformity with the Indenture, and when the Notes have been duly executed, authenticated and issued in accordance with the Indenture and delivered against payment therefor, the Notes will be validly issued and, to the extent validity of the Notes is a matter governed by the laws of the Province of Ontario or Québec, or the laws of Canada applicable therein, and will be valid obligations of the Bank, subject to equitable remedies which may only be granted at the discretion of a court of competent authority, subject to applicable bankruptcy, to rights to indemnity and contribution under the Notes or the Indenture which may be limited by applicable law; to insolvency and other laws of general application affecting creditors’ rights, to limitations under applicable limitations statutes, and to limitations as to the currency in which judgments in Canada may be rendered, as prescribed by the Currency Act (Canada). This opinion is given as of the date hereof and is limited to the laws of the Provinces of Ontario and Québec and the federal laws of Canada applicable thereto. In addition, this opinion is subject to customary assumptions about the Trustee’s authorization, execution and delivery of the Indenture and the genuineness of signatures and certain factual matters, all as stated in the letter of such counsel dated January 8, 2016, which has been filed as Exhibit 5.1 to Royal Bank’s Form 6-K filed with the SEC dated January 8, 2016.

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In the opinion of Morrison & Foerster LLP, when the Notes have been duly completed in accordance with the Indenture and issued and sold as contemplated by the prospectus supplement and the prospectus, the Notes will be valid, binding and enforceable obligations of Royal Bank, entitled to the benefits of the Indenture, subject to applicable bankruptcy, insolvency and similar laws affecting creditors' rights generally, concepts of reasonableness and equitable principles of general applicability (including, without limitation, concepts of good faith, fair dealing and the lack of bad faith). This opinion is given as of the date hereof and is limited to the laws of the State of New York. This opinion is subject to customary assumptions about the Trustee's authorization, execution and delivery of the Indenture and the genuineness of signatures and to such counsel's reliance on the Bank and other sources as to certain factual matters, all as stated in the legal opinion dated January 8, 2016, which has been filed as Exhibit 5.2 to the Bank's Form 6-K dated January 8, 2016.