

whether it would be in its own interest to make the modifications in question. Similarly, when a borrower commits an act of default under a loan agreement, the lender must determine, in its own interest, what action, if any, it wishes to take. Such action might involve foreclosure on the loan, a restructuring of the loan arrangement, or, in some cases as appropriate, no action at all. When a debt investment is shared among Accounts, a decision must be made on behalf of each Account with respect to the action to be taken when a loan modification or loan default situation occurs. In some cases, moreover, it is conceivable that different actions might be desired by different Accounts. Normally, however, only one unified course of action is possible in the situation. Since UBS Realty manages each of the Client Accounts (while the General Account is managed by Aetna), the action the Applicant decides to take for the particular Accounts may raise questions under section 406 of the Act. Accordingly, exemptive relief is being requested that will permit the Applicant on behalf of the Accounts to take appropriate action with respect to the modification of the material terms of a loan, or with respect to a default situation when the loan is a shared investment involving one or more ERISA-Covered Accounts, or with respect to the acquisition of additional debt. Each such action would require approval of the independent fiduciary for each ERISA-Covered Account and the Applicant or the client for each non-ERISA-Covered Client Account. If there is an agreement among the independent fiduciaries and the non-ERISA-Covered Client Accounts as to the course of action to follow with regard to a proposed loan modification, or an adjustment in the rights upon default, such modification or adjustment will be implemented. If, upon full discussion of the matter, no course of action can be agreed upon by the independent fiduciaries and the non-ERISA-Covered Client Accounts, no modification of the terms of the loan or adjustment in the rights upon default would be made. The terms of the loan agreement as originally stated would be carried out. With respect to shared debt investments involving ERISA-Covered Accounts and non-ERISA-Covered Client Accounts, decisions on behalf of the non-ERISA-Covered Accounts will be made by persons independent of Aetna, UBS Realty and any of their respective affiliates. See Section I(e).

## II. Partnership Investments

29. Many real estate investments are structured as partnership arrangements

(rather than 100 percent ownership interest in property) in which the Applicant and another party, such as a real estate developer or manager, participate as co-partners. Generally, the Applicant's co-partner acts as managing partner of the joint venture. The Applicant, in turn, may allocate its interest in the partnership to more than one Account. Partnership investments typically involve several particular features by virtue of the terms and conditions of the partnership agreements that may, when the partnership interest is shared, result in possible violations of section 406 of the Act.

### *(a) Additional Capital Contributions to Joint Ventures*

30. As in the case of investments made entirely by Aetna, partnership real estate investments sometimes require additional operating capital. Typically, the partnership agreements entered into by Aetna and many other real estate investors provide for a capital call by the general partner of the partnership to be made to each partner and that each partner provide the needed capital on a pro rata basis either in the form of an equity contribution or a loan to the partnership. If one partner refuses to contribute its pro rata equity share of the capital call, the other partner(s) may contribute additional capital to cover the short-fall and thereby "squeeze down" the interest in the venture of the non-contributing partner.<sup>10</sup> Alternatively, if sufficient additional capital is not provided by the partners, other financing may be sought or the partnership may be liquidated. In the case of a capital call where Aetna's partnership interest is shared by two or more Accounts, a determination must be made on behalf of each Account participating in the shared investment with respect to whether it is appropriate for the Account to provide its proportionate share of additional capital requested by the partnership. The

<sup>10</sup> In the case of a call for additional capital involving a typical partnership arrangement entered into between parties dealing at arm's-length, the partnership agreement may commonly provide that the equity interest of any non-contributing partner be re-adjusted, or "squeezed down," on a capital interest basis. This involves re-adjusting the equity interests of the partners solely on the basis of the percentage of total capital contributed without taking into account any appreciation on the underlying property. This "capital interest" adjustment can substantially diminish the equity interest of the non-contributing partner in the actual current market value of the underlying property. Thus, this type of re-adjustment is intended to provide an incentive to all partners to make their proportionate capital contributions so that improvements can be made and the operation of a property continued without burdening the other partners.

general rule that the Applicant will follow is that each Account will be given the opportunity to provide its pro rata share of the capital call, but for some Accounts it may be determined to be appropriate to provide less than a full share or no additional capital at all. In such cases, the interest of the Account would be reduced proportionately on a fair market basis. In the case of ERISA-Covered Accounts, all decisions regarding the making of additional capital contributions must be approved by the independent fiduciary for the ERISA-Covered Account. In addition to situations where some Accounts participating in the ownership of Aetna's partnership interest may not be in a position to provide their share of a capital call, other situations may arise where a partner is unable to make its additional capital contributions. Both of these situations may result in prohibited transactions under section 406 of the Act. See Section II(a).

31. *Aetna Shortfall.* In situations where the General Account and an ERISA-Covered Account are sharing an investment in a partnership, the General Account and an ERISA-Covered Account may experience a capital call from the general partner of the partnership for either an additional equity or debt contribution. If it is determined that the ERISA-Covered Account does not have sufficient funds available to meet its contribution requirement,<sup>11</sup> the General Account may make an additional equity contribution to the partnership to cover the ERISA-Covered Account's shortfall. However, in any case where the General Account contributes an ERISA-Covered Account's shortfall, the ERISA-Covered Account's share of the partnership interest will be readjusted and reduced based upon the change in the fair market value of the partnership interest held by Aetna which is caused by the infusion of new capital, thus recognizing any appreciation in the investment. There is no "capital basis squeeze down" effect under these circumstances as there might be under the partnership agreement should Aetna (in its role as a partner) fail to meet a

<sup>11</sup> In any case where the General Account and one or more ERISA-Covered Accounts share Aetna's interest in a partnership, the General Account will always make a capital contribution that is at least equivalent proportionately to the highest capital contribution made by an ERISA-Covered Account (but not higher than the General Account's pro rata share of the required additional capital except, as described in paragraph 30, in the event of a co-venturer shortfall). Thus, as between the Accounts, the General Account will never be the cause of a capital contribution shortfall by Aetna that would result in a capital basis squeeze down by a partner.