



DEPARTMENT OF THE TREASURY  
INTERNAL REVENUE SERVICE  
WASHINGTON, D.C. 20224

OFFICE OF THE CHIEF COUNSEL

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Kevin M. Simpson  
Associate General Counsel for Finance, Procurement and Administrative Law  
U. S. Department of Housing and Urban Development  
Washington, DC 20410-0500  
Attention: Ms. Dana Boyd

Dear Ms. Boyd:

This letter responds to your request dated August 13, 2015, concerning the tax consequences of certain modifications to multifamily loans that collateralize Government National Mortgage Association (GNMA) pass-thru certificates held by real estate mortgage investment conduits (REMICs) guaranteed by GNMA. You requested that the Internal Revenue Service (the Service) confirm that these modifications are not treated as modifications of the GNMA pass-thru certificate, and thus that sections 1.860G-2(b)(1) and 1.860G-2(a)(8) of the Income Tax Regulations (the regulations) do not apply.

HUD Programs

GNMA is a corporation wholly owned by the United States within the Department of Housing and Urban Development (HUD). 12 U.S.C. §1717(a)(2)(A). GNMA expands affordable housing finance in the United States by linking the capital markets to the nation's housing finance markets, providing liquidity to federally sponsored mortgage lending programs.

In furtherance of this objective, GNMA operates a mortgage-backed securities (MBSs) program under which GNMA guarantees investors the timely payment of principal and interest on MBSs issued by approved private lenders and backed by federally insured or guaranteed mortgages (GNMA MBSs). Multifamily and Healthcare GNMA MBSs may be backed by several different multifamily and healthcare loans or may be backed by a single multifamily or healthcare loan. The Multifamily and Healthcare GNMA MBS program helps to finance loans for multifamily housing developments and healthcare facilities, including hospitals, nursing homes, and assisted living facilities.

In addition to its Multifamily and Healthcare GNMA MBS program, GNMA administers a multiclass securities program under which REMIC securities are sold. GNMA guarantees investors the timely payment of principal and interest on the REMIC securities. GNMA REMICs hold GNMA MBSs or previously issued GNMA REMIC securities. The loans backing the GNMA REMIC securities include, but are not limited to, multifamily and healthcare loans insured by the Federal Housing Administration (FHA) or otherwise institutionally guaranteed (by the Department of Agriculture's Rural Development Office).

HUD provides mortgage insurance through FHA pursuant to the National Housing Act. FHA insurance is available for construction, rehabilitation, purchase, and refinance of multifamily housing projects and healthcare facilities. Each FHA insurance program has specific eligibility requirements, including loan to value limits. FHA and its approved lenders must review each mortgage loan, and each borrower request pertaining thereto, to ensure that FHA requirements are satisfied.

#### Modifications of Collateral Descriptions and Changes to Collateral underlying GNMA Securities

FHA reviews requests to modify properties that serve as collateral for existing FHA loans. Partial releases of liens on collateral may be sought, for example, in order to donate or sell parts of a parcel in conjunction with an expansion of rights of way or a conveyance of an outlying parcel to a neighbor. Additions to collateral may also arise if a contiguous parcel is acquired. All partial releases, collateral additions, and other collateral modifications must be reviewed and approved by FHA.

Section 241(a) of the National Housing Act authorizes supplemental loans to finance repairs, additions, and improvements to insured multifamily projects and healthcare facilities. These FHA-insured loans permit existing FHA projects to allow repairs, improvements, enhancements, and modernizations to existing projects. Section 241(a) supplemental loans (section 241 loans) are generally eligible collateral for GNMA securities.

Because a section 241 loan is subordinated to the existing first mortgage, the addition of a section 241 loan in and of itself does not reduce the amount of collateral supporting the existing first mortgage loan. In securing a section 241 loan, however, it is often necessary to amend the legal description of the collateral securing the first mortgage loan, or to make other accommodating changes to that loan. FHA reviews these modifications of collateral descriptions in the process of insuring a section 241 loan.

## Section 1.860G-2 of the Regulations

### 1. Obligations Secured by Interests in Real Property

Obligations principally secured by interests in real property are qualified mortgages under section 860G(a)(3)(A) of the Internal Revenue Code (Code). In order to qualify as a REMIC, substantially all of the assets of an entity must consist of qualified mortgages and permitted investments under section 860D(a)(4).

Section 1.860G-2(a)(5) of the regulations provides, in pertinent part, that obligations secured by interests in real property include pass-thru certificates guaranteed by GNMA. This regulation goes on to list other obligations that meet the definition of obligations secured by interests in real property. Included in this list are "obligations secured by manufactured housing treated as single family residences [under relevant statutory authority.]"

GNMA has asked whether the application of section 1.860G-2(a)(5) is limited to a pass-thru certificate guaranteed by GNMA that is backed by single family loans, or whether it also applies to a pass-thru certificate guaranteed by GNMA that is backed by multifamily loans.

### 2. Modifications of Mortgage Loans and Release of Liens

Section 1.860G-2(b)(1) of the regulations provides that, except as elsewhere specifically excepted, if there is a significant modification of an obligation held by a REMIC, the modified obligation is treated as one that was newly issued in exchange for the unmodified obligation that it replaced. Thus, even if an entity initially qualified as a REMIC, one or more significant modifications of loans held by the entity may terminate the entity's qualification if the modifications cause less than substantially all of the entity's assets to be qualified mortgages and permitted investments. See section 860D(a)(4) of the Code.

Section 1.860G-2(b)(6) of the regulations provides that, if a REMIC holds as a qualified mortgage a pass-thru certificate or investment trust interest of the type described in paragraph (a)(5) of this section, the modification of a mortgage loan that backs the pass-thru certificate or other interest is not a modification of the pass-thru certificate or other interest unless the investment trust structure was created to avoid the prohibited transaction rules of section 860F(a) of the Code. Section 860F(a) imposes a tax on income derived from certain prohibited transactions entered into by a REMIC, including the disposition of a qualified mortgage.

Section 1.860G-2(a)(8) of the regulations provides that if a REMIC releases its lien on an interest in real property that secures a qualified mortgage, that mortgage ceases to be a qualified mortgage on the date the lien is released unless the REMIC releases its

lien in a modification that either is not a significant modification under the regulations, or falls within one of the listed exceptions in the regulations.

Assuming that a pass-thru certificate guaranteed by GNMA that is backed by multifamily loans is an "obligation secured by interests in real property" under section 1.860G-2(a)(5), GNMA has asked whether such certificate remains a qualified mortgage under section 1.860G-2(b) and section 1.860G-2(a)(8) of the regulations if there are modifications or additions to collateral or partial releases of liens on the collateral for the mortgage loans ("Modifications") that back the certificate.

### 3. Revenue Procedure 2010-30

Revenue Procedure 2010-30, 2010-36 I.R.B. 316, describes the circumstances under which the Service will not challenge a mortgage loan held by a REMIC as other than a qualified mortgage on the grounds that the mortgage loan fails to be principally secured by an interest in real property for purposes of section 860G(a)(3)(A) of the Code and section 1.860G-2(a)(8) of the regulations following a release of a lien on an interest in real property that secures the mortgage loan. Section 4.10 of the revenue procedure provides that the modification of a mortgage loan that backs a pass-through certificate or other interest is not a modification of the pass-through certificate or other interest unless the investment trust structure that holds the loan was created to avoid the REMIC prohibited transaction rules. Analogously, the revenue procedure further provides that the release of a lien on an interest in real property that secures an obligation does not cause section 1.860G-2(a)(8) automatically to disqualify the obligation unless a substantial purpose of the trust structure that holds the obligation is to avoid the restrictions imposed by section 1.860G-2(a)(8) and section 1.860G-2(b).

GNMA has represented that the GNMA MBS program and the GNMA REMIC program were not created to avoid the REMIC prohibited transaction rules of section 860(F)(a) of the Code or the lien release rules in section 1.860G-2(a)(8) of the regulations. The language of section 1.860G-2(a)(5) that provides that pass-thru certificates guaranteed by GNMA are obligations secured by interests in real property is not limited to pass-thru certificates backed by single family loans. That language also applies to pass-thru certificates backed by multifamily loans. Therefore, the Modifications to multifamily loans that back GNMA pass-thru certificates would not be considered modifications of the pass-thru certificates under either section 1.860G-2(b)(6) of the regulations or Rev. Proc. 2010-30, and thus sections 1.860G-2(b)(1) and 1.860G-2(a)(8) of the regulations do not apply.

This letter calls your attention to certain general principles of tax law. It is intended for informational purposes only, does not constitute a letter ruling, and has no binding effect on the Service. See Rev. Proc. 2015-1, 2015-1 I.R.B. 1, § 2.04. If you have any additional questions, please contact the undersigned at (202) 317-4414 or Susan Baker at (202) 317-4421.

Sincerely,

A handwritten signature in blue ink, appearing to read "D.B. Silber".

David B. Silber  
Deputy Associate Chief Counsel  
(Financial Institutions & Products)