

Internal Revenue Service, Treasury

§ 301.7701(i)-1

shall be excluded for individuals described in §301.7701(b)-3(b)(5) (professional athletes).

(4) *Procedural rules and filing requirements.* The procedural rules and filing requirements described in §§301.7701(b)-7(b) and 301.7701(b)-8 shall apply to taxable years beginning after December 31, 1991.

(5) *Possessions and territories.* For purposes of applying section 7701(b) and the regulations under that section, §301.7701(b)-1(d) applies to taxable years ending after April 9, 2008.

[T.D. 8411, 57 FR 15253, Apr. 27, 1992, as amended by T.D. 9391, 73 FR 19377, Apr. 9, 2008]

§ 301.7701(i)-0 Outline of taxable mortgage pool provisions.

This section lists the major paragraphs contained in §§301.7701(i)-1 through 301.7701(i)-4.

§ 301.7701(i)-1 Definition of a taxable mortgage pool.

- (a) Purpose.
- (b) In general.
- (c) Asset composition tests.
 - (1) Determination of amount of assets.
 - (2) Substantially all.
 - (i) In general.
 - (ii) Safe harbor.
 - (3) Equity interests in pass-through arrangements.
 - (4) Treatment of certain credit enhancement contracts.
 - (i) In general.
 - (ii) Credit enhancement contract defined.
 - (5) Certain assets not treated as debt obligations.
 - (i) In general.
 - (ii) Safe harbor.
 - (A) In general.
 - (B) Payments with respect to a mortgage defined.
 - (C) Entity treated as not anticipating payments.
 - (d) Real estate mortgages or interests therein defined.
 - (1) In general.
 - (2) Interests in real property and real property defined.
 - (i) In general.
 - (ii) Manufactured housing.
 - (3) Principally secured by an interest in real property.
 - (i) Tests for determining whether an obligation is principally secured.
 - (A) The 80 percent test.
 - (B) Alternative test.
 - (ii) Obligations secured by real estate mortgages (or interests therein), or by com-

binations of real estate mortgages (or interests therein) and other assets.

- (A) In general.
- (B) Example.
- (e) Two or more maturities.
 - (1) In general.
 - (2) Obligations that are allocated credit risk unequally.
- (3) Examples.
- (f) Relationship test.
 - (1) In general.
 - (2) Payments on asset obligations defined.
 - (3) Safe harbor for entities formed to liquidate assets.
- (g) Anti-avoidance rules.
 - (1) In general.
 - (2) Certain investment trusts.
 - (3) Examples.

§ 301.7701(i)-2 Special rules for portions of entities.

- (a) Portion defined.
- (b) Certain assets and rights to assets disregarded.
 - (1) Credit enhancement assets.
 - (2) Assets unlikely to service obligations.
 - (3) Recourse.
 - (c) Portion as obligor.
 - (1) In general.
 - (2) Example.

§ 301.7701(i)-3 Effective dates and duration of taxable mortgage pool classification.

- (a) Effective dates.
- (b) Entities in existence on December 31, 1991.
 - (1) In general.
 - (2) Special rule for certain transfers.
 - (3) Related debt obligation.
 - (4) Example.
- (c) Duration of taxable mortgage pool classification.
 - (1) Commencement and duration.
 - (2) Testing day defined.

§ 301.7701(i)-4 Special rules for certain entities.

- (a) States and municipalities.
 - (1) In general.
 - (2) Governmental purpose.
 - (3) Determinations by the Commissioner.
- (b) REITs. [Reserved]
- (c) Subchapter S corporations.
 - (1) In general.
 - (2) Portion of an S corporation treated as a separate corporation.

[T.D. 8610, 60 FR 40088, Aug. 7, 1995]

§ 301.7701(i)-1 Definition of a taxable mortgage pool.

(a) *Purpose.* This section provides rules for applying section 7701(i), which defines taxable mortgage pools. The purpose of section 7701(i) is to prevent income generated by a pool of real estate mortgages from escaping Federal

income taxation when the pool is used to issue multiple class mortgage-backed securities. The regulations in this section and in §§ 301.7701(i)-2 through 301.7701(i)-4 are to be applied in accordance with this purpose. The taxable mortgage pool provisions apply to entities or portions of entities that qualify for REMIC status but do not elect to be taxed as REMICs as well as to certain entities or portions of entities that do not qualify for REMIC status.

(b) *In general.* (1) A taxable mortgage pool is any entity or portion of an entity (as defined in § 301.7701(i)-2) that satisfies the requirements of section 7701(i)(2)(A) and this section as of any testing day (as defined in § 301.7701(i)-3(c)(2)). An entity or portion of an entity satisfies the requirements of section 7701(i)(2)(A) and this section if substantially all of its assets are debt obligations, more than 50 percent of those debt obligations are real estate mortgages, the entity is the obligor under debt obligations with two or more maturities, and payments on the debt obligations under which the entity is obligor bear a relationship to payments on the debt obligations that the entity holds as assets.

(2) Paragraph (c) of this section provides the tests for determining whether substantially all of an entity's assets are debt obligations and for determining whether more than 50 percent of its debt obligations are real estate mortgages. Paragraph (d) of this section defines real estate mortgages for purposes of the 50 percent test. Paragraph (e) of this section defines two or more maturities and paragraph (f) of this section provides rules for determining whether debt obligations bear a relationship to the assets held by an entity. Paragraph (g) of this section provides anti-avoidance rules. Section 301.7701(i)-2 provides rules for applying section 7701(i) to portions of entities and § 301.7701(i)-3 provides effective dates. Section 301.7701(i)-4 provides special rules for certain entities. For purposes of the regulations under section 7701(i), the term entity includes a portion of an entity (within the meaning of section 7701(i)(2)(B)), unless the context clearly indicates otherwise.

(c) *Asset composition tests*—(1) *Determination of amount of assets.* An entity must use the Federal income tax basis of an asset for purposes of determining whether substantially all of its assets consist of debt obligations (or interests therein) and whether more than 50 percent of those debt obligations (or interests) consist of real estate mortgages (or interests therein). For purposes of this paragraph, an entity determines the basis of an asset with the assumption that the entity is not a taxable mortgage pool.

(2) *Substantially all*—(i) *In general.* Whether substantially all of the assets of an entity consist of debt obligations (or interests therein) is based on all the facts and circumstances.

(ii) *Safe harbor.* Notwithstanding paragraph (c)(2)(i) of this section, if less than 80 percent of the assets of an entity consist of debt obligations (or interests therein), then less than substantially all of the assets of the entity consist of debt obligations (or interests therein).

(3) *Equity interests in pass-through arrangements.* The equity interest of an entity in a partnership, S corporation, trust, REIT, or other pass-through arrangement is deemed to have the same composition as the entity's share of the assets of the pass-through arrangement. For example, if an entity's stock interest in a REIT has an adjusted basis of \$20,000, and the assets of the REIT consist of equal portions of real estate mortgages and other real estate assets, then the entity is treated as holding \$10,000 of real estate mortgages and \$10,000 of other real estate assets.

(4) *Treatment of certain credit enhancement contracts*—(i) *In general.* A credit enhancement contract (as defined in paragraph (c)(4)(ii) of this section) is not treated as a separate asset of an entity for purposes of the asset composition tests set forth in section 7701(i)(2)(A)(i), but instead is treated as part of the asset to which it relates. Furthermore, any collateral supporting a credit enhancement contract is not treated as an asset of an entity solely because it supports the guarantee represented by that contract.

(ii) *Credit enhancement contract defined.* For purposes of this section, a

credit enhancement contract is any arrangement whereby a person agrees to guarantee full or partial payment of the principal or interest payable on a debt obligation (or interest therein) or on a pool of such obligations (or interests), or full or partial payment on one or more classes of debt obligations under which an entity is the obligor, in the event of defaults or delinquencies on debt obligations, unanticipated losses or expenses incurred by the entity, or lower than expected returns on investments. Types of credit enhancement contracts may include, but are not limited to, pool insurance contracts, certificate guarantee insurance contracts, letters of credit, guarantees, or agreements whereby an entity, a mortgage servicer, or other third party agrees to make advances (regardless of whether, under the terms of the agreement, the payor is obligated, or merely permitted, to make those advances). An agreement by a debt servicer to advance to an entity out of its own funds an amount to make up for delinquent payments on debt obligations is a credit enhancement contract. An agreement by a debt servicer to pay taxes and hazard insurance premiums on property securing a debt obligation, or other expenses incurred to protect an entity's security interests in the collateral in the event that the debtor fails to pay such taxes, insurance premiums, or other expenses, is a credit enhancement contract.

(5) *Certain assets not treated as debt obligations*—(i) *In general*. For purposes of section 7701(i)(2)(A), real estate mortgages that are seriously impaired are not treated as debt obligations. Whether a mortgage is seriously impaired is based on all the facts and circumstances including, but not limited to: the number of days delinquent, the loan-to-value ratio, the debt service coverage (based upon the operating income from the property), and the debtor's financial position and stake in the property. However, except as provided in paragraph (c)(5)(ii) of this section, no single factor in and of itself is determinative of whether a loan is seriously impaired.

(ii) *Safe harbor*—(A) *In general*. Unless an entity is receiving or anticipates receiving payments with respect to a

mortgage, a single family residential real estate mortgage is seriously impaired if payments on the mortgage are more than 89 days delinquent, and a multi-family residential or commercial real estate mortgage is seriously impaired if payments on the mortgage are more than 59 days delinquent. Whether an entity anticipates receiving payments with respect to a mortgage is based on all the facts and circumstances.

(B) *Payments with respect to a mortgage defined*. For purposes of paragraph (c)(5)(ii)(A) of this section, payments with respect to a mortgage mean any payments on the mortgage as defined in paragraph (f)(2)(i) of this section if those payments are substantial and relatively certain as to amount and any payments on the mortgage as defined in paragraph (f)(2) (ii) or (iii) of this section.

(C) *Entity treated as not anticipating payments*. With respect to any testing day (as defined in §301.7701(i)-3(c)(2)), an entity is treated as not having anticipated receiving payments on the mortgage as defined in paragraph (f)(2)(i) of this section if 180 days after the testing day, and despite making reasonable efforts to resolve the mortgage, the entity is not receiving such payments and has not entered into any agreement to receive such payments.

(d) *Real estate mortgages or interests therein defined*—(1) *In general*. For purposes of section 7701(i)(2)(A)(i), the term real estate mortgages (or interests therein) includes all—

(i) Obligations (including participations or certificates of beneficial ownership therein) that are principally secured by an interest in real property (as defined in paragraph (d)(3) of this section);

(ii) Regular and residual interests in a REMIC; and

(iii) Stripped bonds and stripped coupons (as defined in section 1286(e) (2) and (3)) if the bonds (as defined in section 1286(e)(1)) from which such stripped bonds or stripped coupons arose would have qualified as real estate mortgages or interests therein.

(2) *Interests in real property and real property defined*—(i) *In general*. The definition of interests in real property set forth in §1.856-3(c) of this chapter and

the definition of real property set forth in §1.856-3(d) of this chapter apply to define those terms for purposes of paragraph (d) of this section.

(ii) *Manufactured housing.* For purposes of this section, the definition of real property includes manufactured housing, provided the properties qualify as single family residences under section 25(e)(10) and without regard to the treatment of the properties under state law.

(3) *Principally secured by an interest in real property—(i) Tests for determining whether an obligation is principally secured.* For purposes of paragraph (d)(1) of this section, an obligation is principally secured by an interest in real property only if it satisfies either the test set out in paragraph (d)(3)(i)(A) of this section or the test set out in paragraph (d)(3)(i)(B) of this section.

(A) *The 80 percent test.* An obligation is principally secured by an interest in real property if the fair market value of the interest in real property (as defined in paragraph (d)(2) of this section) securing the obligation was at least equal to 80 percent of the adjusted issue price of the obligation at the time the obligation was originated (that is, the issue date). For purposes of this test, the fair market value of the real property interest is first reduced by the amount of any lien on the real property interest that is senior to the obligation being tested, and is reduced further by a proportionate amount of any lien that is in parity with the obligation being tested.

(B) *Alternative test.* An obligation is principally secured by an interest in real property if substantially all of the proceeds of the obligation were used to acquire, improve, or protect an interest in real property that, at the origination date, is the only security for the obligation. For purposes of this test, loan guarantees made by Federal, state, local governments or agencies, or other third party credit enhancement, are not viewed as additional security for a loan. An obligation is not considered to be secured by property other than real property solely because the obligor is personally liable on the obligation.

(ii) *Obligations secured by real estate mortgages (or interests therein), or by*

combinations of real estate mortgages (or interests therein) and other assets—(A) In general. An obligation secured only by real estate mortgages (or interests therein), as defined in paragraph (d)(1) of this section, is treated as an obligation secured by an interest in real property to the extent of the value of the real estate mortgages (or interests therein). An obligation secured by both real estate mortgages (or interests therein) and other assets is treated as an obligation secured by an interest in real property to the extent of both the value of the real estate mortgages (or interests therein) and the value of so much of the other assets that constitute real property. Thus, under this paragraph, a collateralized mortgage obligation may be an obligation principally secured by an interest in real property. This section is applicable only to obligations issued after December 31, 1991.

(B) *Example.* The following example illustrates the principles of this paragraph (d)(3)(ii):

Example. At the time it is originated, an obligation has an adjusted issue price of \$300,000 and is secured by a \$70,000 loan principally secured by an interest in a single family home, a fifty percent co-ownership interest in a \$400,000 parcel of land, and \$80,000 of stock. Under paragraph (d)(3)(ii)(A) of this section, the obligation is treated as secured by interests in real property and under paragraph (d)(3)(i)(A) of this section, the obligation is treated as principally secured by interests in real property.

(e) *Two or more maturities—(1) In general.* For purposes of section 7701(i)(2)(A)(ii), debt obligations have two or more maturities if they have different stated maturities or if the holders of the obligations possess different rights concerning the acceleration of or delay in the maturities of the obligations.

(2) *Obligations that are allocated credit risk unequally.* Debt obligations that are allocated credit risk unequally do not have, by that reason alone, two or more maturities. Credit risk is the risk that payments of principal or interest will be reduced or delayed because of a default on an asset that supports the debt obligations.

(3) *Examples.* The following examples illustrate the principles of this paragraph (e):

Example 1. (i) Corporation M transfers a pool of real estate mortgages to a trustee in exchange for Class A bonds and a certificate representing the residual beneficial ownership of the pool. All Class A bonds have a stated maturity of March 1, 2002, but if cash flows from the real estate mortgages and investments are sufficient, the trustee may select one or more bonds at random and redeem them earlier.

(ii) The Class A bonds do not have different maturities. Each outstanding Class A bond has an equal chance of being redeemed because the selection process is random. The holders of the Class A bonds, therefore, have identical rights concerning the maturities of their obligations.

Example 2. (i) Corporation N transfers a pool of real estate mortgages to a trustee in exchange for Class C bonds, Class D bonds, and a certificate representing the residual beneficial ownership of the pool. The Class D bonds are subordinate to the Class C bonds so that cash flow shortfalls due to defaults or delinquencies on the real estate mortgages are borne first by the Class D bond holders. The terms of the bonds are otherwise identical in all relevant aspects except that the Class D bonds carry a higher coupon rate because of the subordination feature.

(ii) The Class C bonds and the Class D bonds share credit risk unequally because of the subordination feature. However, neither this difference, nor the difference in interest rates, causes the bonds to have different maturities. The result is the same if, in addition to the other terms described in paragraph (i) of this *Example 2*, the Class C bonds are accelerated as a result of the issuer becoming unable to make payments on the Class C bonds as they become due.

(f) *Relationship test*—(1) *In general.* For purposes of section 7701(i)(2)(A)(iii), payments on debt obligations under which an entity is the obligor (liability obligations) bear a relationship to payments (as defined in paragraph (f)(2) of this section) on debt obligations an entity holds as assets (asset obligations) if under the terms of the liability obligations (or underlying arrangement) the timing and amount of payments on the liability obligations are in large part determined by the timing and amount of payments or projected payments on the asset obligations. For purposes of the relationship test, any payment arrangement, including a swap or other hedge, that achieves a substantially similar result is treated as satisfying the test. For example, any arrangement where the timing and amount of payments on li-

ability obligations are determined by reference to a group of assets (or an index or other type of model) that has an expected payment experience similar to that of the asset obligations is treated as satisfying the relationship test.

(2) *Payments on asset obligations defined.* For purposes of section 7701(i)(2)(A)(iii) and this section, payments on asset obligations include—

(i) A payment of principal or interest on an asset obligation, including a prepayment of principal, a payment under a credit enhancement contract (as defined in paragraph (c)(4)(ii) of this section) and a payment from a settlement at a discount (other than a substantial discount);

(ii) A payment from a settlement at a substantial discount, but only if the settlement is arranged, whether in writing or otherwise, prior to the issuance of the liability obligations; and

(iii) A payment from the foreclosure on or sale of an asset obligation, but only if the foreclosure or sale is arranged, whether in writing or otherwise, prior to the issuance of the liability obligations.

(3) *Safe harbor for entities formed to liquidate assets.* Payments on liability obligations of an entity do not bear a relationship to payments on asset obligations of the entity if—

(i) The entity's organizational documents manifest clearly that the entity is formed for the primary purpose of liquidating its assets and distributing proceeds of liquidation;

(ii) The entity's activities are all reasonably necessary to and consistent with the accomplishment of liquidating assets;

(iii) The entity plans to satisfy at least 50 percent of the total issue price of each of its liability obligations having a different maturity with proceeds from liquidation and not with scheduled payments on its asset obligations; and

(iv) The terms of the entity's liability obligations (or underlying arrangement) provide that within three years of the time it first acquires assets to be liquidated the entity either—

(A) Liquidates; or

(B) Begins to pass through without delay all payments it receives on its asset obligations (less reasonable allowances for expenses) as principal payments on its liability obligations in proportion to the adjusted issue prices of the liability obligations.

(g) *Anti-avoidance rules*—(1) *In general.* For purposes of determining whether an entity meets the definition of a taxable mortgage pool, the Commissioner can disregard or make other adjustments to a transaction (or series of transactions) if the transaction (or series) is entered into with a view to achieving the same economic effect as that of an arrangement subject to section 7701(i) while avoiding the application of that section. The Commissioner's authority includes treating equity interests issued by a non-REMIC as debt if the entity issues equity interests that correspond to maturity classes of debt.

(2) *Certain investment trusts.* Notwithstanding paragraph (g)(1) of this section, an ownership interest in an entity that is classified as a trust under § 301.7701-4(c) will not be treated as a debt obligation of the trust.

(3) *Examples.* The following examples illustrate the principles of this paragraph (g):

Example 1. (i) Partnership P, in addition to its other investments, owns \$10,000,000 of mortgage pass-through certificates guaranteed by FNMA (FNMA Certificates). On May 15, 1997, Partnership P transfers the FNMA Certificates to Trust 1 in exchange for 100 Class A bonds and Certificate 1. The Class A bonds, under which Trust 1 is the obligor, have a stated principal amount of \$5,000,000 and bear a relationship to the FNMA Certificates (within the meaning of § 301.7701(i)-1(f)). Certificate 1 represents the residual beneficial ownership of the FNMA Certificates.

(ii) On July 5, 1997, with a view to avoiding the application of section 7701(i), Partnership P transfers Certificate 1 to Trust 2 in exchange for 100 Class B bonds and Certificate 2. The Class B bonds, under which Trust 2 is the obligor, have a stated principal amount of \$5,000,000, bear a relationship to the FNMA Certificates (within the meaning of § 301.7701(i)-1(f)), and have a different maturity than the Class A bonds (within the meaning of § 301.7701(i)-1(e)). Certificate 2 represents the residual beneficial ownership of Certificate 1.

(iii) For purposes of determining whether Trust 1 is classified as a taxable mortgage

pool, the Commissioner can disregard the separate existence of Trust 2 and treat Trust 1 and Trust 2 as a single trust.

Example 2. (i) Corporation Q files a consolidated return with its two wholly-owned subsidiaries, Corporation R and Corporation S. Corporation R is in the business of building and selling single family homes. Corporation S is in the business of financing sales of those homes.

(ii) On August 10, 1998, Corporation S transfers a pool of its real estate mortgages to Trust 3, taking back Certificate 3 which represents beneficial ownership of the pool. On September 25, 1998, with a view to avoiding the application of section 7701(i), Corporation R issues bonds that have different maturities (within the meaning of § 301.7701(i)-1(e)) and that bear a relationship (within the meaning of § 301.7701(i)-1(f)) to the real estate mortgages in Trust 3. The holders of the bonds have an interest in a credit enhancement contract that is written by Corporation S and collateralized with Certificate 3.

(iii) For purposes of determining whether Trust 3 is classified as a taxable mortgage pool, the Commissioner can treat Trust 3 as the obligor of the bonds issued by Corporation R.

Example 3. (i) Corporation X, in addition to its other assets, owns \$110,000,000 in Treasury securities. From time to time, Corporation X acquires pools of real estate mortgages, which it immediately uses to issue multiple-class debt obligations.

(ii) On October 1, 1996, Corporation X transfers \$20,000,000 in Treasury securities to Trust 4 in exchange for Class C bonds, Class D bonds, Class E bonds, and Certificate 4. Trust 4 is the obligor of the bonds. The different classes of bonds have the same stated maturity date, but if cash flows from the Trust 4 assets exceed the amounts needed to make interest payments, the trustee uses the excess to retire the classes of bonds in alphabetical order. Certificate 4 represents the residual beneficial ownership of the Treasury securities.

(iii) With a view to avoiding the application of section 7701(i), Corporation X reserves the right to replace any Trust 4 asset with real estate mortgages or guaranteed mortgage pass-through certificates. In the event the right is exercised, cash flows on the real estate mortgages and guaranteed pass-through certificates will be used in the same manner as cash flows on the Treasury securities. Corporation X exercises this right of replacement on February 1, 1997.

(iv) For purposes of determining whether Trust 4 is classified as a taxable mortgage pool, the Commissioner can treat February 1, 1997, as a testing day (within the meaning of § 301.7701(i)-3(c)(2)). The result is the same if Corporation X has an obligation, rather than a right, to replace the Trust 4 assets

with real estate mortgages and guaranteed pass-through certificates.

Example 4. (i) Corporation Y, in addition to its other assets, owns \$1,900,000 in obligations secured by personal property. On November 1, 1995, Corporation Y begins negotiating a \$2,000,000 loan to individual A. As security for the loan, A offers a first deed of trust on land worth \$1,700,000.

(ii) With a view to avoiding the application of section 7701(i), Corporation Y induces A to place the land in a partnership in which A will have a 95 percent interest and agrees to accept the partnership interest as security for the \$2,000,000 loan. Thereafter, the loan to A, together with the \$1,900,000 in obligations secured by personal property, are transferred to Trust 5 and used to issue bonds that have different maturities (within the meaning of § 301.7701(i)-1(e)) and that bear a relationship (within the meaning of § 301.7701(i)-1(f)) to the \$1,900,000 in obligations secured by personal property and the loan to A.

(iii) For purposes of determining whether Trust 5 is a taxable mortgage pool, the Commissioner can treat the loan to A as an obligation secured by an interest in real property rather than as an obligation secured by an interest in a partnership.

Example 5. (i) Corporation Z, in addition to its other assets, owns \$3,000,000 in notes secured by interests in retail shopping centers. Partnership L, in addition to its other assets, owns \$20,000,000 in notes that are principally secured by interests in single family homes and \$3,500,000 in notes that are principally secured by interests in personal property.

(ii) On December 1, 1995, Partnership L asks Corporation Z for two separate loans, one in the amount of \$9,375,000 and another in the amount of \$625,000. Partnership L offers to collateralize the \$9,375,000 loan with \$10,312,500 of notes secured by interests in single family homes and the \$625,000 loan with \$750,000 of notes secured by interests in personal property. Corporation Z has made similar loans to Partnership L in the past.

(iii) With a view to avoiding the application of section 7701(i), Corporation Z induces Partnership L to accept a single \$10,000,000 loan and to post as collateral \$7,500,000 of the notes secured by interests in single family homes and all \$3,500,000 of the notes secured by interests in personal property. Ordinarily, Corporation Z would not make a loan on these terms. Thereafter, the loan to Partnership L, together with the \$3,000,000 in notes secured by interests in retail shopping centers, are transferred to Trust 6 and used to issue bonds that have different maturities (within the meaning of § 301.7701(i)-1(e)) and that bear a relationship (within the meaning of § 301.7701(i)-1(f)) to the loans secured by interests in retail shopping centers and the loan to Partnership L.

(iv) For purposes of determining whether Trust 6 is a taxable mortgage pool, the Commissioner can treat the \$10,000,000 loan to Partnership L as consisting of a \$9,375,000 obligation secured by interests in real property and a \$625,000 obligation secured by interests in personal property. Under § 301.7701(i)-1(d)(3)(ii)(A), the notes secured by single family homes are treated as \$7,500,000 of interests in real property. Under § 301.7701(i)-1(d)(3)(i)(A), \$7,500,000 of interests in real property are sufficient to treat a \$9,375,000 obligation as principally secured by an interest in real property (\$7,500,000 equals 80 percent of \$9,375,000).

[T.D. 8610, 60 FR 40088, Aug. 7, 1995; 60 FR 49754, Sept. 27, 1995]

§ 301.7701(i)-2 Special rules for portions of entities.

(a) *Portion defined.* Except as provided in paragraph (b) of this section and § 301.7701(i)-1, a portion of an entity includes all assets that support one or more of the same issues of debt obligations. For this purpose, an asset supports a debt obligation if, under the terms of the debt obligation (or underlying arrangement), the timing and amount of payments on the debt obligation are in large part determined, either directly or indirectly, by the timing and amount of payments or projected payments on the asset or a group of assets that includes the asset. Indirect payment arrangements include, for example, a swap or other hedge, or arrangements where the timing and amount of payments on the debt obligations are determined by reference to a group of assets (or an index or other type of model) that has an expected payment experience similar to that of the assets. For purposes of this paragraph, the term payments includes all proceeds and receipts from an asset.

(b) *Certain assets and rights to assets disregarded—(1) Credit enhancement assets.* An asset that qualifies as a credit enhancement contract (as defined in § 301.7701(i)-1(c)(4)(ii)) is not included in a portion as a separate asset, but is treated as part of the assets in the portion to which it relates under § 301.7701(i)-1(c)(4)(i). An asset that does not qualify as a credit enhancement contract (as defined in § 301.7701(i)-1(c)(4)(ii)), but that nevertheless serves the same function as a credit enhancement contract, is not included in a portion as a separate asset or otherwise.