ALSTON + BIRD LLP

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IRS Will Not Challenge REMIC Status for Certain Loan Modifications Made in Connection with the Home Affordable Modification Program

On April 10, 2009, the Internal Revenue Service (IRS) issued Revenue Procedure 2009-23[1] (the "Revenue Procedure") and Notice 2009-36 (the "Notice"),[2] to provide guidance regarding the effects of the Home Affordable Modification Program (HAMP) on real estate mortgage investment conduits (REMICs) and certain trusts. HAMP is a key component of the Homeowner Affordability and Stability Plan, which is aimed at preventing foreclosure for at-risk homeowners. HAMP provides guidelines for the identification of homeowners who are at high risk of defaulting on their residential mortgage loans, by analyzing factors such as the ratio of their mortgage debt to their monthly income. Once identified, HAMP provides incentives to lenders and servicers of the securitizations in which such loans are held (such as a REMIC or an investment trust) to modify these loans so that the monthly payments are consistent with the program's desired debt-to-income ratios.

The Notice states that the IRS and the Treasury Department will issue regulations to address the potential disconnect between the REMIC provisions (specifically, Section 860G(d) of the Internal Revenue Code of 1986, as amended (the "Code")) and payments made to lenders under HAMP. Absent such regulations, payments made to a lender under HAMP could be subject to a 100 percent tax under Section 860G(d)(1) of the Code, which, with certain exceptions, prohibits contributions to a REMIC after its startup day. Until the issuance of such regulations, taxpayers are permitted to rely on the Notice for the proposition that HAMP payments to lenders will not be subject to this 100 percent tax.

The Revenue Procedure addresses modifications made to loans pursuant to the HAMP guidelines that could otherwise potentially jeopardize the tax status of a REMIC or investment trust. Specifically, the IRS will not challenge the tax status of such securitization vehicles if a loan modification is made pursuant to HAMP. Furthermore, the IRS will not assert that such modifications will result in the application of the 100 percent prohibited transactions tax, or otherwise be treated as a re-issuance of either the REMIC's loans or its regular interests. Absent the Revenue Procedure, a lender would potentially subject the income from a modified mortgage loan to a 100 percent tax and risk losing REMIC status if a modification made to a loan is considered a significant modification under the REMIC provisions.

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1 Rev. Proc. 2009-23, 2009-17 IRB.

2 Notice 2009-36, 2009-17 IRB.

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Conclusion

In the current economic environment, the Revenue Procedure and Notice provide comfort and useful guidance to the securitization industry on certain tax consequences of electing to participate in HAMP. However, servicers and lenders should take note that the Revenue Procedure only provides such guidance with respect to modifications made pursuant to HAMP guidelines, and does not address the effect of modifications made to loans pursuant to other foreclosure prevention programs.[3]

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3 The IRS has provided guidance on other foreclosure prevention programs in Revenue Procedure 2008-47, 2008-31 IRB 272, and Revenue Procedure 2008-28, 2008-23 IRB 1054.

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