an obligation on or after September 16, 2009.

[T.D. 8458, 57 FR 61300, Dec. 24, 1992; 58 FR 8098, Feb. 11, 1993; 58 FR 15089, Mar. 19, 1993; T.D. 8614, 60 FR 42787, Aug. 17, 1995; T.D. 9272, 71 FR 43365, Aug. 1, 2006; T.D. 9415, 73 FR 40172, July 14, 2008; T.D. 9463, 74 FR 47438, Sept. 16, 2009]

§ 1.860C–1 Taxation of holders of residual interests.

(a) *Pass-thru of income or loss.* Any holder of a residual interest in a REMIC must take into account the holder's daily portion of the taxable income or net loss of the REMIC for each day during the taxable year on which the holder owned the residual interest.

(b) *Adjustments to basis of residual interests*—(1) *Increase in basis.* A holder's basis in a residual interest is increased by—

(i) The daily portions of taxable income taken into account by that holder under section 860C(a) with respect to that interest; and

(ii) The amount of any contribution described in section 860G(d)(2) made by that holder.

(2) *Decrease in basis.* A holder's basis in a residual interest is reduced (but not below zero) by—

(i) First, the amount of any cash or the fair market value of any property distributed to that holder with respect to that interest; and

(ii) Second, the daily portions of net loss of the REMIC taken into account under section 860C(a) by that holder with respect to that interest.

(3) *Adjustments made before disposition.* If any person disposes of a residual interest, the adjustments to basis prescribed in paragraph (b) (1) and (2) of this section are deemed to occur immediately before the disposition.

(c) *Counting conventions.* For purposes of determining the daily portion of REMIC taxable income or net loss under section 860C(a)(2), any reasonable convention may be used. An example of a reasonable convention is ''30 days per month/90 days per quarter/360 days per year.''

(d) For rules on the proper accounting for income from inducement fees, *see* § 1.446–6.

[T.D. 8458, 57 FR 61301, Dec. 24, 1992, as amended by T.D. 9128, 69 FR 26041, May 11, 2004]

§ 1.860C–2 Determination of REMIC taxable income or net loss.

(a) *Treatment of gain or loss.* For purposes of determining the taxable income or net loss of a REMIC under section 860C(b), any gain or loss from the disposition of any asset, including a qualified mortgage (as defined in section 860G(a)(3)) or a permitted investment (as defined in section 860G(a)(5) and § 1.860G–2(g)), is treated as gain or loss from the sale or exchange of property that is not a capital asset.

(b) *Deductions allowable to a REMIC*—(1) *In general.* Except as otherwise provided in section 860C(b) and in paragraph (b) (2) through (5) of this section, the deductions allowable to a REMIC for purposes of determining its taxable income or net loss are those deductions that would be allowable to an individual, determined by taking into account the same limitations that apply to an individual.

(2) *Deduction allowable under section 163.* A REMIC is allowed a deduction, determined without regard to section 163(d), for any interest expense accrued during the taxable year.

(3) *Deduction allowable under section 166.* For purposes of determining a REMIC's bad debt deduction under section 166, debt owed to the REMIC is not treated as nonbusiness debt under section 166(d).

(4) *Deduction allowable under section 212.* A REMIC is not treated as carrying on a trade or business for purposes of section 162. Ordinary and necessary operating expenses paid or incurred by the REMIC during the taxable year are deductible under section 212, without regard to section 67. Any expenses that are incurred in connection with the formation of the REMIC and that relate to the organization of the REMIC and the issuance of regular and residual interests are not treated as expenses of the REMIC for which a deduction is allowable under section 212. See § 1.860F–2(b)(3)(ii) for treatment of those expenses.

(5) *Expenses and interest relating to tax-exempt income.* Pursuant to section 265(a), a REMIC is not allowed a deduction for expenses and interest allocable to tax-exempt income. The portion of a REMIC's interest expense that is allocable to tax-exempt interest is determined in the manner prescribed in section 265(b)(2), without regard to section 265(b)(3).

[T.D. 8458, 57 FR 61301, Dec. 24, 1992]

§ 1.860D–1 Definition of a REMIC.

(a) *In general.* A real estate mortgage investment conduit (or REMIC) is a qualified entity, as defined in paragraph (c)(3) of this section, that satisfies the requirements of section 860D(a). See paragraph (d)(1) of this section for the manner of electing REMIC status.

(b) *Specific requirements*—(1) *Interests in a REMIC*—(i) *In general.* A REMIC must have one class, and only one class, of residual interests. Except as provided in paragraph (b)(1)(ii) of this section, every interest in a REMIC must be either a regular interest (as defined in section 860G(a)(1) and §1.860G–1(a)) or a residual interest (as defined in section 860G(a)(2) and §1.860G–1(c)).

(ii) *De minimis interests.* If, to facilitate the creation of an entity that elects REMIC status, an interest in the entity is created and, as of the startup day (as defined in section 860G(a)(9) and §1.860G–2(k)), the fair market value of that interest is less than the lesser of $1,000 or 1/1,000 of one percent of the aggregate fair market value of all the regular and residual interests in the REMIC, then, unless that interest is specifically designated as an interest in the REMIC, the interest is not treated as an interest in the REMIC for purposes of section 860D(a) (2) and (3) and paragraph (B)(1)(i) of this section.

(2) *Certain rights not treated as interests.* Certain rights are not treated as interests in a REMIC. Although not an exclusive list, the following rights are not interests in a REMIC.

(i) *Payments for services.* The right to receive from the REMIC payments that represent reasonable compensation for services provided to the REMIC in the ordinary course of its operation is not an interest in the REMIC. Payments made by the REMIC in exchange for services may be expressed as a specified percentage of interest payments due on qualified mortgages or as a specified percentage of earnings from permitted investments. For example, a mortgage servicer's right to receive reasonable compensation for servicing the mortgages owned by the REMIC is not an interest in the REMIC.

(ii) *Stripped interests.* Stripped bonds or stripped coupons not held by the REMIC are not interests in the REMIC even if, in a transaction preceding or contemporaneous with the formation of the REMIC, they and the REMIC's qualified mortgages were created from the same mortgage obligation. For example, the right of a mortgage servicer to receive a servicing fee in excess of reasonable compensation from payments it receives on mortgages held by a REMIC is not an interest in the REMIC. Further, if an obligation with a fixed principal amount provides for interest at a fixed or variable rate and for certain contingent payment rights (*e.g.*, a shared appreciation provision or a percentage of mortgagor profits provision), and the owner of the obligation contributes the fixed payment rights to a REMIC and retains the contingent payment rights, the retained contingent payment rights are not an interest in the REMIC.

(iii) *Reimbursement rights under credit enhancement contracts.* A credit enhancer's right to be reimbursed for amounts advanced to a REMIC pursuant to the terms of a credit enhancement contract (as defined in §1.860G–2 (c)(2)) is not an interest in the REMIC even if the credit enhancer is entitled to receive interest on the amounts advanced.

(iv) *Rights to acquire mortgages.* The right to acquire or the obligation to purchase mortgages and other assets from a REMIC pursuant to a clean-up call (as defined in §1.860G–2(j)) or a qualified liquidation (as defined in section 860F(a)(4)), or on conversion of a convertible mortgage (as defined in §1.860G–2(d)(5)), is not an interest in the REMIC.

(3) *Asset test*—(i) *In general.* For purposes of the asset test of section