

# Comfort Letters, Rent Insurance and Mortgages

By James F. McDonough, Jr. on April 2nd, 2012 Posted in Assets, Estate Planning, Estates, Real Estate, Tax Return

The real estate market, in severe decline over the last few years, has shown signs of life recently. Naturally, the supervising government agencies, lenders, and loan brokers are sensitive to avoiding the mistakes of the past and have implemented new requirements to prevent any repeat of errors. Here are two new items that have come to light.

1) Comfort Letters. Lenders and loan brokers are requesting “comfort letters” from accountants in connection with loan applications of individuals. This focuses upon the most common accountant-client relationship, where the preparation of an individual income tax return is the only service involved. In furtherance of this service, the accountant sends a questionnaire that is completed by the client and returned along with Forms W-2 and 1099. The accountant does not audit or verify the information. One state accountancy board has taken the position that the issuance of such a letter is an attestation service that requires certain accounting procedures to be followed. The New Jersey Society recommends that the accountant contact his or her insurance carrier before making a decision on whether or not to reply. Accountants are told by clients and lenders that the loan will not be approved without the Comfort Letter. I am also advised that the accountants are being instructed on what language the letter must contain. An individual borrower would be wise to inquire of the lender or loan broker whether a comfort letter will be required of his accountant before paying an application fee.

2) Rent Insurance & Mortgages. The second issue that has come to our attention is rather odd. A lender, refinancing its purchase money mortgage for a condominium located in a New Jersey beach community, insisted that the mortgage include a 1-4 multi-family rider. The inconsistency is that the rider requires the homeowner to obtain rent insurance for its vacation home. I am assured that rent insurance is not available where the second home is occupied by the owner-mortgagor. What makes this interesting is that the Second Home Rider absolutely prohibits rental to a third party for the life of the loan. Upon executing the Mortgage that includes these two riders, the owner agrees not to rent the condominium and to only use it as a second home while immediately obtaining rent insurance for the tenant he cannot have. The lender blamed the investor, that is the government, for this requirement and insisted that it will not enforce the requirement that rent insurance be obtained. The lender will not respond to the question as to whether it can bind the investor.

If these items are any indication, the transition to a more vibrant market will be bumpy.