



## **IS YOUR COLLATERAL REALLY INSURED?**

The procedures for assuring that property insurance is maintained for mortgage loans and other loans secured by real estate may seem like a routine matter, but our experience tells us otherwise. BancInsure recently paid a claim due to a lapse in insurance coverage on property pledged as collateral after a fire destroyed the building on the property.

In 1996 a couple, we will call them Mr. and Ms. Jones, acquired a parcel of real estate. It was approximately two acres in size and there was a two-story structure located on it. The first floor was utilized as a service station and convenience store with the second floor being used as the Jones' residence. In early 2000, the bank refinanced the Jones's debt from another institution in the approximate amount of \$170,000. The property appraised at \$300,000. Shortly after the refinancing the couple began divorce proceedings. In July of 2000 the debt was re-financed in Ms. Jones' name only. In August of 2000 the structure on the property suffered a major fire. The authorities determined that the fire was arson, but their investigation cleared Mr. and Ms. Jones of any involvement or knowledge of the arson. After the fire the bank learned that the structure was not insured. It seems that at the July 2000 loan closing that Ms. Jones made the verbal representation or assurance that she would deliver a binder or certificate of insurance verifying the existence of property insurance the next morning. She did not do so. The loan records were transmitted to the processing center for data entry. Once the data entry was completed, the loan documents were sent to the files. No tickler or note to the effect of the lack of evidence of insurance was made. As a result, insurance coverage was not procured for the property.

After the fire the bank learned that the original appraisal of \$300,000 was in error as the underground storage tanks and pumping stations was leased property and were not available as a source of recovery. The mortgage and security agreement did not include personal property located on the second floor, but included commercial personal property such as equipment, fixtures and inventory. BancInsure offers mortgage bankers' errors and omissions endorsements to several bond and policies that provide coverage for loss of mortgage interest in real property. The bank had purchased one of these endorsements. BancInsure paid \$100,656 after the application of the \$1,000 deductible on the claim based on the cash value estimate. The borrower was unable to continue to make payments. The bank foreclosed on the mortgage and recovery of most of the remaining loss will be achieved through the proceeds from the sale of the foreclosed property.

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