The Basics of UCC Insurance

by Theodore Sprink, SVP, UCC Insurance Division, FNF

The recently developed concept of UCC insurance has become a checklist item for most major mezzanine investors and lenders, oftentimes driven by secondary market considerations. Loans insured by UCC insurance and sold into the secondary market tend to have greater value than those loans that are not insured.

Most major commercial real estate transactions have a mezzanine component built into the capital structure of the deal. A mezzanine loan is often considered a bridge loan, and appears in some respects as a subordinate loan secured by a second trust deed on the real property.

However, a mezzanine loan, by definition, is located in the capital stack above the senior debt and below the equity. Hence, the word mezzanine refers generally to the "middle." A mezzanine loan is generally secured by the borrower's pledge of its ownership interest, or a pledge of equity in the entity that owns the entity that owns the real estate project.

The "pledge" is personal property, as defined by Articles 8 and 9 of the Uniform Commercial Code, and is therefore insured by UCC insurance, not traditional real estate title insurance. In recent years, it is not uncommon for the mezzanine component to be 15 to 25 percent of the overall capital structure of a large commercial real estate project.

The title industry developed UCC insurance in order to provide lenders and investors who were collateralized with non-real estate personal property with the benefits of title insurance, initially specializing in mezzanine loans. Such insurance provided certain coverages and shifted risk for non-real estate lenders in much the same way that they generally did in the real estate world. Since its introduction, the title industry has produced approximately $450 billion in UCC insurance policies.

UCC insurance is a "collateral protection" title insurance product that insures the lender's security interest in loans secured by non-real estate assets for validity, enforceability, attachment, perfection and priority. UCC insurance covers fraud and forgery; insures the gap; and provides cost-of-defense coverage in the event of a third-party challenge to the lender's lien priority.

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UCC insurance protects against documentation defects, UCC search office indexing problems, financing statement inaccuracies and search office errors and omissions. Policies include UCC search and filing services and are life-of-loan.

Although UCC insurance is a relative newcomer to the financial markets, lenders and investors are poised to gain many of the same benefits of traditional title insurance currently and prominently enjoyed in the real estate markets.

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About the Author ...

Ted Sprink is SVP for the UCC Insurance division of the Fidelity National Financial Family of Companies and is one of the original architects of the concept of UCC insurance. He can be reached at 760.931.4731 or **tsprink@fnf.com**. Additional details about UCCPlus can be found at **www.uccplus.com**.