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Why building owners should have Contingent Operation of Building Laws coverage

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Most commercial property owners feel content and secure that their property insurance will fully and adequately cover them in the event of an insured loss. They purchase Special Form perils and replacement cost valuation, and the more astute buyer also gets coinsurance waived via the Agreed Amount endorsement. But they may not realize that, lurking in plain sight within their policy, there are two universal provisions that might be their undoing.

Property insurance will pay for the damage caused by a covered peril loss, with the recovery dependent upon the valuation clause: if ACV, then depreciation is deducted; if replacement cost, it will be the cost to repair or replace with like kind and quality. These are not threatening concepts and they seem to be good, kind, and straightforward. However, it is what is not said that is the problem.

Suppose, for example, that you have a six story building that sustains a major fire that consumes the first two floors, affecting the structural integrity of the entire building. The city or state, after inspecting the remaining portion of the building, proclaims it unsafe and mandates demolition of the entire building. You intend to replace the entire building "as is." What will your insurance claim look like?

You will seek to be paid for the cost to replace the entire building. Your insurer will agree to pay for the replacement value of the first two floors, provided you actually replace them; otherwise, you will collect their depreciated value. You inquire about the top four floors and are told that they were not damaged by the fire, and consequently they are not covered. Remember, your property insurance pays for the actual physical damage caused by a covered peril.

You have just discovered why you need Contingent Operation of Building Laws (COBL) coverage, aka Building Ordinance coverage. Unfortunately, you have discovered this after the fire. This coverage is actually an extension of your building coverage and limit and will pay for the value of the undamaged portion of your property should the enforcement of a building law or ordinance result in your having to tear that part down as a result of that covered peril loss.

To add insult to injury, your insurer will also tell you that the cost to tear down the undamaged portion and remove the debris isn't covered under your typical building coverage either. This demolition expense is a second component of the COBL coverage unit.

The final straw is when you learn, now that your building with its grandfathered codes is gone, that

you will need to sprinker the new building and install elevators and other ADA-related features, and your insurer has that last conversation where they tell you that none of that will be covered, either, since the policy will pay to repair or replace with like kind and quality and you cannot rebuild "as is." This increased cost of construction is the third component of the COBL coverage unit.

As mentioned, when you include COBL in your building coverage you will gain coverage for the value of the undamaged portion in the event of a covered peril loss. Typically, you will select sublimits for the demolition and increased cost of construction components, and you can purchase these separately or combined under one sublimit. Be aware, however, that some insurers offer a very limited amount of COBL cover, making it imperative that you and your agent ensure that you are getting the coverage and limits you need.

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