

The Ordinance or Law Endorsement

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Generally speaking, the Ordinance or Law Endorsement is meant to provide some additional protection in circumscribed situations, not to pay for upgrades.

Ordinance or Law Coverage in Connection with Direct Physical Loss and Code Upgrades

The standard commercial property insurance policy does not cover loss or damage resulting from the enforcement of an ordinance or law regulating the construction, use, repair, or demolition of a building. The standard policy

excludes coverage for undamaged portions of the building and the “increased costs incurred to comply with an ordinance or law in the course of construction, repair, renovation, remodeling or demolition of property, or removal of its debris, following a physical loss to that property.”

If an insured chooses to purchase optional replacement-cost coverage, the standard commercial property insur-

ance policy provides additional coverage for increased costs of construction. In an optional replacement cost coverage policy, the typical language reads: “we will pay the increased costs incurred to comply with the minimum standards of an ordinance or law in the course of repair, rebuilding or replacement of damaged parts of that property.” However, that coverage is limited to the lesser of \$10,000, or five percent of the

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limit of insurance applicable to the subject covered building.

Commercial property insurance policies can also be specifically endorsed to provide broader coverage for repair of undamaged portions of a building and increased costs of construction that result from enforcement of ordinances or laws relating to the construction, repair, or demolition of property. Cov-

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erage provided by these endorsements may not cover costs to remedy code violations that are not directly related to the physical damage; update undamaged portions of the property to current standards, even when the update is necessary to repair the direct physical loss; or make code-related repairs that are only discovered incidental to the loss, such as preexisting code violations.

The Role of Ordinance or Law Coverage

In the event of damage to a building, costs incurred to repair the building may extend beyond those attributed solely to repairing the direct physical damage as a consequence of having to comply with existing code. The increased costs may result from the need to rebuild damaged portions of the building in compliance with current code, or to demolish undamaged but non-compliant portions of the building and rebuild them to code standards. In gen-

eral, ordinance or law coverage may provide an insured with coverage for upgrades required by code where a portion of a structure is damaged due to a covered, direct, physical loss, and in order to proceed with repairs to the property—whether damaged or undamaged—that portion needs to be upgraded due to intervening changes in code since original construction.

Whether by way of a manuscript endorsement or the standardized Insurance Services Office (ISO) Ordinance or Law Coverage Endorsement, a typical ordinance or law endorsement provides one or more of the following three categories of coverage: coverage for loss to the undamaged portion of the building; coverage for demolition and clearing of undamaged parts of the building; and coverage for the increased costs of construction. Coverage is usually triggered by direct physical loss caused by a covered cause of loss, and repairs to the undamaged portion of the building, demolition, or increased costs to reconstruct the damaged or undamaged portions of the building are “a consequence of a requirement to comply with an ordinance or law” that governs the repair, construction, or demolition of buildings.

The coverage usually also requires demolition of a portion of the building to trigger the coverage; thus, if the direct physical loss can be repaired without demolishing any portion of the building, then the coverage would not be triggered. If, however, a building inspector required that an undamaged portion of the building be brought into compliance with current code—and that, in turn, required demolition of the undamaged portion of the building—then, depending on the specific language of the endorsement, ordinance, or law, coverage would likely be triggered to provide coverage for the cost to demolish the undamaged portion and repair it to code standards. A good example of this are losses involving only a part of a building “system”—such as losses in which only a portion of a roof, one of several support structures, or one exterior wall is damaged—which typically give rise to the need to demolish and bring the undamaged parts of the partially damaged roof, support system, or walls into compliance with current code.

Disputes Regarding the Scope of Ordinance or Law Coverage

The scope of coverage provided by the limited additional increased cost of construction coverage provided by optional replacement cost policies is rarely controversial. Similarly, the line between what is and is not covered under a triggered policy endorsed to include ordinance or law coverage is typically easier to discern where a building suffers a covered loss and either (1) a preexisting code violation is discovered during repairs, which must be remedied to complete the repairs to the damaged portion of the building; or (2) the code upgrade is clearly not related to the direct physical loss.

Disputes most often arise when only a small portion of a building system, such as a section of roof, is damaged, and to repair that structure, an undamaged portion of the building needs to be brought into compliance with existing code. In the roof example, that could mean the walls supporting the roof. Disputes also arise where a latent code violation unrelated to the covered loss is discovered during inspection. Less common, though more significant, litigation may arise where a portion of a property is damaged, but as a result, an entire structure or other buildings must be updated.

Repairs to Undamaged Portions of a Building System or Adjoining Building System

In assessing coverage for repairs to undamaged portions of a building system or adjoining building system, courts generally assess whether there is a nexus between the need to repair the undamaged portion of a building and the direct physical loss. In *Tocci Building Corporation v. Zurich American Insurance Company*, 659 F. Supp. 2d 251 (D. Mass. 2009), for example, a rainstorm caused damage to less than one hundred feet of a 1,200-foot retaining wall. The town declared the wall unsafe and discovered that it had not been built in accordance with the original plans. The insured had to grout the entire wall after the loss and argued that the grouting should be considered a continuation of the work done on the damaged section of the wall. The court determined the storm and resulting damage was merely the event that brought the wall to the inspector’s attention, but there was no physical damage or

loss that led to the requirement of grouting the entire wall. Absent a causal connection between the loss and the additional grouting work, the court declined to extend coverage to the grouting work.

The court reached a similar conclusion in *CV Ice Company v. Golden Eagle Insurance Company*, No. CV 14-121 PSG (SPx), 2015 U.S. Dist. Lexis 1070 (C.D. Cal. Jan. 6, 2015). In *CV Ice Company*, the insured's ice-making system was enclosed in a steel tank, and the tank was punctured by an angle iron, resulting in the release of ammonia. An engineer concluded that the damage could be fixed with a weld repair, but the inspector found that the system violated the health and safety code. The court held that the covered loss did not trigger the code violation in any way other than putting the inspector on notice of the problematic condition. In so holding, the court acknowledged that the policy provision did not explicitly state that the covered loss must trigger enforcement of a law requiring the demolition of undamaged property to be covered, but it was "the only logical interpretation of the provision," and "[i]f a causation requirement is not read into the [Ordinance or Law] Coverage provision, the results are absurd."

On the other hand, in *DEB Associates v. Greater New York Mutual Insurance Company*, 970 A.2d 1074 (N.J. Super. Ct. App. Div. 2009), a windstorm damaged the brick facade, concrete perimeter wall, and some windows of a building. An inspection revealed that the walls were secured to the flooring using a mortar rather than a steel angle iron throughout the building, and the walls were no longer securely attached to the flooring. Municipal code officials concluded the building was not safe unless it was brought up to current code standards. The court held that there was a clear causal connection between the collapse of the seventh floor wall and the code officials' mandate that the remaining floors be brought into compliance to prevent them from collapsing. Consequently, the court found that the insured was entitled to coverage for those repairs.

Repairs of Latent or Preexisting Code Violations Discovered During Post-Loss Inspections

In many instances, a covered loss prompts an investigation that reveals additional

code violations. Despite that most courts recognize the need for some physical connection between the direct physical loss and the undamaged property to be upgraded, some courts have required insurers to provide coverage for code upgrades to portions of properties not even indirectly affected by a direct physical loss.

The most common rationale of courts finding coverage for code upgrades seemingly unrelated to a covered cause of loss is that the requirement to provide coverage is a "consequence" of the requirement to comply with an ordinance or law, not a consequence of the covered loss. This logic is based on policy language providing that an insurer will pay for the cost to upgrade undamaged portions of a building, or the increased costs of construction, as "a consequence of a requirement to comply with an ordinance or law." Thus, courts sometimes find coverage to correct latent code violations discovered only during post-loss inspections.

In *City of Elmira v. Selective Insurance Company of New York*, 921 N.Y.S.2d 662 (2011), a three-story building was damaged by windstorm that caused a portion of its southern wall to collapse. The condition was caused by the deterioration of the mortar, which weakened the wall before the storm, and it was recommended that the building be vacated until the exterior walls were rebuilt. The owner of the building elected to have the building demolished and sought coverage to demolish and clear the site of the undamaged parts. The court rejected the insurer's position that the endorsement could not be invoked because a covered cause of loss did not cause the enforcement of the code requiring the building to be renovated or demolished. Rather, the court found that the ordinance or law provision did not contain such a requirement: it required only that (1) a covered case of loss occur, and (2) the plaintiff incur costs to demolish and clear the site of undamaged parts of the property as a result of an ordinance or law. The only causal link required under the provision was that the costs to demolish the undamaged portion be caused by enforcement of an ordinance or law.

The court reached a similar conclusion in *Davidson Hotel Company v. St. Paul Fire & Marine Insurance Company*, 136 F.

Supp. 2d 901 (W.D. Tenn. 2001). In *Davidson*, water caused damage when it infiltrated a bus duct in the electrical room of a hotel. Inspectors subsequently required compliance with numerous building code provisions as a condition to completing the repairs. The court held that the insurer was liable for the costs associated with compliance with the provisions because the inspection would not have occurred but for the incident. Similarly, in *Commonwealth Insurance Company v. Benihana of Tokyo*, No. 3:96-CV-0826-R, 1997 U.S. Dist. Lexis 17448 (N.D. Tex. 1997), an insured sought indemnification after a restaurant fire for fixing the damaged and undamaged portions of the building. The court held that the endorsement was applicable because the inspection of the restaurant, and the subsequent enforcement of the code, was triggered by the fire in the restaurant.

Nevertheless, despite cases extending coverage to latent violations not caused by the covered loss, most courts still emphasize the importance of the causal connection between the covered loss and the enforcement of an ordinance or law. In other words, even though a covered loss might prompt an investigation that leads to the discovery of ordinance violations, most courts still conclude that there is no coverage because the covered loss did not cause the enforcement of the ordinance or law. A good example of this rationale is the case of *St. George Tower v. Insurance Company of Greater New York*, 139 A.D.3d 200 (N.Y. App. Div. 2016). In that case, pressure testing of a pump resulted in a flood that damaged ceilings and floors in certain apartments. During the course of remediation, it was discovered that concrete slabs under the flooring needed to be repaired. The insured sought coverage despite the fact that it was stipulated that the flooding did not cause the damage. Although the policy itself did not contain a causation requirement, the court read such a requirement into the language. Its basis for doing so was that the ordinance or law endorsement "cannot be triggered simply by the discovery, in the course of an inspection necessitated by a covered event, of structural problems that amount to code violations." The court in *Sanderson v. First Liberty Insurance Corporation*, 2019 U.S. Dist. Lexis 76494 (N.D.N.Y.

May 7, 2019), relied on *St. George Tower* in holding that an insurer was not responsible for the electrical work in the insured's home that needed to be brought up to code before water-caused damage could be remedied. The court concluded that this case was analogous to *St. George Tower* because "there, as here, the shoddy work that must now be upgraded to meet code is wholly

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unrelated to the water damage covered by the homeowner's policy." See also *St. Paul Fire & Marine Ins. Co. v. Darlak Motor Inns, Inc.*, No. 3:97-CV-1559 TIV, 1999 U.S. Dist. Lexis 23283 (M.D. Pa. Mar. 9, 1999), *aff'd*, 205 F.3d 1330 (3d Cir. 1999) (holding that costs to remedy code violations discovered during post-loss inspections in portions of a hotel undamaged by a fire were not covered because they were not the result of damage done by the fire, and the fire loss did not cause the enforcement of any laws or ordinances); *61 Jane St. Tenants Corporation v. Great American Insurance Company*, No. 00 CIV. 1049 (GEL), 2001 U.S. Dist. Lexis 265 (S.D.N.Y. Jan. 17, 2001) ("the fact that the violations would have gone undetected but for the fire would not turn

the cost of complying with the code into a fire loss.").

Most ordinance or law endorsements, including the ISO form, exclude coverage for ordinances or laws that "you were required to comply with before the time of the current loss, even in the absence of building damage, if you failed to comply." This language narrows the scope of a covered loss to exclude preexisting code violations, while still allowing for coverage in accordance with consumer expectations to the extent that the insured may be "grandfathered in" regarding certain violations where they must comply with code after the loss negates the grandfathered compliance. The dispute that arises under this policy language usually relates to whether the code violation preexisted the loss, such as in the case of "shoddy" construction, or whether grandfather status was lost because of the occurrence of covered damage. See generally *Chattanooga Bank Assocs. v. Fid. & Deposit Co. of Maryland*, 301 F. Supp. 2d 774, 779-80 (E.D. Tenn. 2004) (holding that the insurer was not responsible for code violations that did not result from the fire, noting that it would not "be consistent with the public policy concern for public safety to permit a building owner to insure against the discovery of existing code violations.").

To that end, the insurer is typically not responsible if the insured was never in compliance with an ordinance, code, or law. In *Estate of Hauser v. Westchester Surplus Lines Insurance Company*, No. CIV.A. 13-5631, 2015 U.S. Dist. Lexis 26499 (E.D. La. Mar. 4, 2015), several properties sustained damage resulting from a hurricane. The court determined that the insurer was not responsible for the costs to bring the walls into compliance because they were not compliant before the hurricane. (The wall was never in compliance with the International Building Code or the American Society of Civil Engineers Minimum Design Loads for Buildings and Other Structures.) Accordingly, the court held that the insurer was not required to incur additional costs to bring the walls into compliance with an ordinance or law that it was not compliant with at the time of the storm. Similarly, in *Celebrate Windsor, Inc. v. Harleysville Worcester Ins. Co.*, No. 3:05CV282 (MRK), 2006 U.S. Dist. Lexis 27043 (D. Conn. May 2, 2006), the canopy

of a performing arts center collapsed, due to snow, and it was determined that the canopy was not properly built in the first place. The court found the insurer was not responsible for incurring increased costs to remedy design defects in the preexisting structure.

Courts are also reluctant to afford coverage where the insured was previously informed of a violation but failed to correct it. In *Rock-N-Rolls Auto Salon, Inc. v. United States Fidelity & Guarantee Company*, 2006 N.J. Super. Unpub. Lexis 2439 (N.J. Sup. Ct. May 31, 2006), a fire damaged a carwash and a dispute ensued over the installation of a "zero-discharge system." An inspector had issued a series of notices to the insured of violations stemming from the illegal discharge, yet the insured had not installed the system as of the date of the fire. The court held that coverage was excluded because the insured was required to comply with the inspector's notices before the fire, even if the building was undamaged.

Repairs to Entire Properties or Structures

Less common are disputes involving whether damage to a part of a property can trigger coverage for extensive repairs to other covered properties. In one particularly extreme example, *Houston Specialty Insurance Company v. Meadows West Condo Association*, 640 F. App'x 267 (5th Cir. 2016), two units in a single condominium building were damaged by fire. A fire department investigation determined the layout of duct work and maintenance issues could have contributed to the fire. The insurer paid the claim for the building that sustained fire damage but refused to cover the work in the seventeen undamaged buildings. The court held that all of the buildings were covered because the policy defined "Building(s)" as "the buildings or other structures at the Insured Location." The court determined that this definition made it so the singular term "building" referred to all buildings at the property.

In contrast, a different court found no ordinance or law coverage where an insured sought coverage for repairs to a sixty-five-mile pipeline where only a small stretch of pipeline was damaged but the inspector mandated testing and repair to the entire pipeline. *MarkWest Hydrocar-*

bon, Inc. v. Liberty Mut. Ins. Co., 558 F.3d 1184 (10th Cir. 2009). A pressure build-up caused the release of gas through a hole that caught fire. The office of pipeline safety undertook an investigation, which required the insured to take corrective action on the entire pipeline. The court held that the insurer was not responsible for the costs simply because the accident exposed problems to the inspector: “[t]o read the policy as covering MarkWest’s costs of complying with safety regulations would be to convert the parties’ policy against unforeseen fortuities into a maintenance contract.”

Conclusion

Though the scope of coverage may differ, depending on the wording of the particular policy language and developed jurisprudence, the triggering by direct physical loss of ordinance or law coverage for undamaged portions of a building presents a unique conundrum. Discerning whether upgrades to undamaged portions of a building—or entirely different buildings covered by the same policy—are covered under an ordinance or law endorsement can present scope and interpretational issues.

While the ordinance or law endorsement provides an insured with an additional layer of protection for losses caused by the enforcement of ordinances or laws regulating the repair, reconstruction, or demolition of a property, it is not blanket coverage intended to allow an insured to upgrade every building system after a covered loss to a portion of a building. Such a broad application of the coverage would result in a world in which the insurer is always on the proverbial hook for poor, original construction, or the owner’s failure to maintain the property. 