

Given the Business

BY LAWRENCE SAVELL

As we have explored in prior columns, the question of whether car collecting is a "hobby" or a "business" can have important tax implications. But the question can have significance to car collectors in other contexts as well.

For example, the status of such activities may be critical in determining whether coverage for an incident is provided by an insurance policy. Such a question was presented in *Allstate Insurance Company v. Crouch*, decided on October 27, 1995 by the Supreme Court of New Hampshire.

Robert Crouch and Raymond Smith were friends who shared an interest in restoring and repairing old cars of their own and of their friends. In 1986 or 1987, Crouch and Smith formed R&R Auto, an unincorporated partnership, to take advantage of dealers' price discounts and depreciate their tools for tax purposes. They performed R&R's auto body repair work in an attached two-door garage at Smith's home. In addition to housing R&R, the garage contained some of the Smiths' personal items; Smith worked on his own vehicles there.

Under the R&R name, Crouch and Smith took on auto body work for customers to raise funds for their own automotive hobbies, including restoring their own vehicles. R&R had business cards and letterhead for customers' estimates, and occasionally purchased promotional items featuring the R&R name. Profits in the R&R checking account that exceeded \$2,000 were divided equally between Crouch and Smith. Proceeds were also used to purchase tools for R&R, which Crouch depreciated on his personal tax returns as R&R business assets. Other proceeds went into a fund for Crouch and Smith to buy parts for their personal vehicles. R&R had gross business receipts of more than \$10,000 in 1988, and \$13,000 in 1989. In 1990, it grossed \$36,000, with 45-50 paying customers.


On March 18, 1991, a fire occurred in the Smiths' garage while Crouch was welding a frame on a pickup truck owned by Smith. Welding sparks ignited combustible materials used for auto body repair work on the shop floor and also burned through oxyacetylene gas lines to propane tanks, which exploded. The cost of renting the tanks and providing electricity to the garage had been paid with R&R funds.

The fire destroyed the Smiths' garage, their home, and all contents. After paying for their losses, the Smiths' homeowner's insurance carrier, New England Guaranty, instituted a subrogation (*i.e.*, repayment) action against Crouch, who was defended by Allstate, pursuant to Crouch's personal homeowner's policy. Crouch's Allstate policy included a "business pursuits" exclusion: "We do not cover bodily injury or property damage arising out of the past or present business activities of an insured person." The policy defined "business" as "any full or part-time activity of any kind engaged in for economic gain and the use of any part of any premises for such purposes."

Allstate filed a petition for declaratory judgment, seeking a determination that Crouch's welding activity was a business activity excluded from coverage under the business pursuits exclusion. The trial court disagreed, ruling that because Crouch was engaged in the non-profit activity of restoring Smith's pickup truck when the fire started, his conduct was without profit motive and therefore did not qualify as a business pursuit; thus, the exclusion was inapplicable and the Allstate policy provided coverage. Allstate appealed.

The Supreme Court reversed. It began its analysis by noting that, under New Hampshire law, an insurer bears the burden of proving lack of coverage. The parties had agreed that the definition of "business pursuit" focused on two significant elements: profit motive and continuity. The court ruled that here, these elements were met: the automotive repair work of R&R constituted business activities within the policy exclusion.

The court rejected the argument — adopted by courts in some other jurisdictions — that where the particular injury-causing activity was not for profit, even though the insured was engaged in conduct of the type done by his business, the business pursuits exclusion was inapplicable. It noted that "[f]or exclusion purposes, the focus is on the business pursuit itself, not the specific acts complained of." Here, it observed, "[t]he business pursuit was the profitable automotive repair business. The injury-causing activity was the type of work that R&R Auto customarily performed. That on the particular occasion at issue the work was performed gratuitously does not take it outside the business pursuits exclusion."

The court conceded that "[t]he general rule is that the court will honor the reasonable expectations of the policy holder," and that "[i]t may be reasonable for an insured to expect coverage under a homeowner's policy for damage resulting from occasionally engaging in personal hobbies. But once the hobby has been transformed into a part-time business, as in this case, with close to 50 customers, annual gross revenue of \$36,000, and tools and equipment commensurate with such an operation, it is unreasonable to expect that the insurer has agreed to cover such a risk. We hold that the business pursuits exclusion applies to preclude coverage." 

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