Art and collecting

Building a meaningful legacy

UBS

On the cover:
Sarah Meyohas
Liquid Speculation 3, 2021
Chromogenic print
UBS Art Collection
Courtesy of the artist and C O U N T Y, Palm Beach

Contents

Art Advisory
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Family Advisory and Philanthropy
Nicole Sebastian
Debra Phares
Julie Binder

Advanced Planning
David Leibell
Lora Cicconi
Jacqueline Denton

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This is a UBS Americas publication.

UBS centers of excellence

UBS serves high net worth and ultra high net worth individuals, families and family offices across the globe by connecting clients to expertise, advice and customized solutions—from across the firm and around the world.

Art Advisory guides individuals and families toward the principles and best practices to build, maintain and plan for exceptional lasting collections. Through a suite of advisory services related to art collecting, art market due diligence, collection management and art legacy, collectors of significant wealth are equipped with the knowledge and support to set the standard for our generation's leading collections.

Family Advisory and Philanthropy Services serves as a thought-partner to families of exceptional financial success by providing advice and solutions on topics critical for families to flourish for generations. These topics include intentional communication and decision-making, generational transitions, family wealth education, family governance, and creating meaningful philanthropic legacies to maximize impact locally, nationally and globally.

The **Advanced Planning Group** consists of former practicing estate planning and tax attorneys with extensive private practice experience and diverse areas of specialization, including estate planning strategies, income and transfer tax planning, family office structuring, business succession planning, charitable planning and family governance. The Advanced Planning Group provides comprehensive planning and sophisticated advice and education to ultra high net worth (UHNW) clients of the firm. The Advanced Planning Group also serves as a think tank for the firm, providing thought leadership and creating a robust intellectual capital library on estate planning, tax and related topics of interest to UHNW families.

Family Office Solutions is a team of specialists that exclusively works with USD 100 million+ net worth families and family offices. The team helps clients navigate the challenges and opportunities across their family enterprises, including their businesses, family offices, philanthropic structures, and passions and interests. Having this expertise under one roof allows for integration and layering of services across the UBS ecosystem, delivering a personalized, holistic client experience.

Executive summary

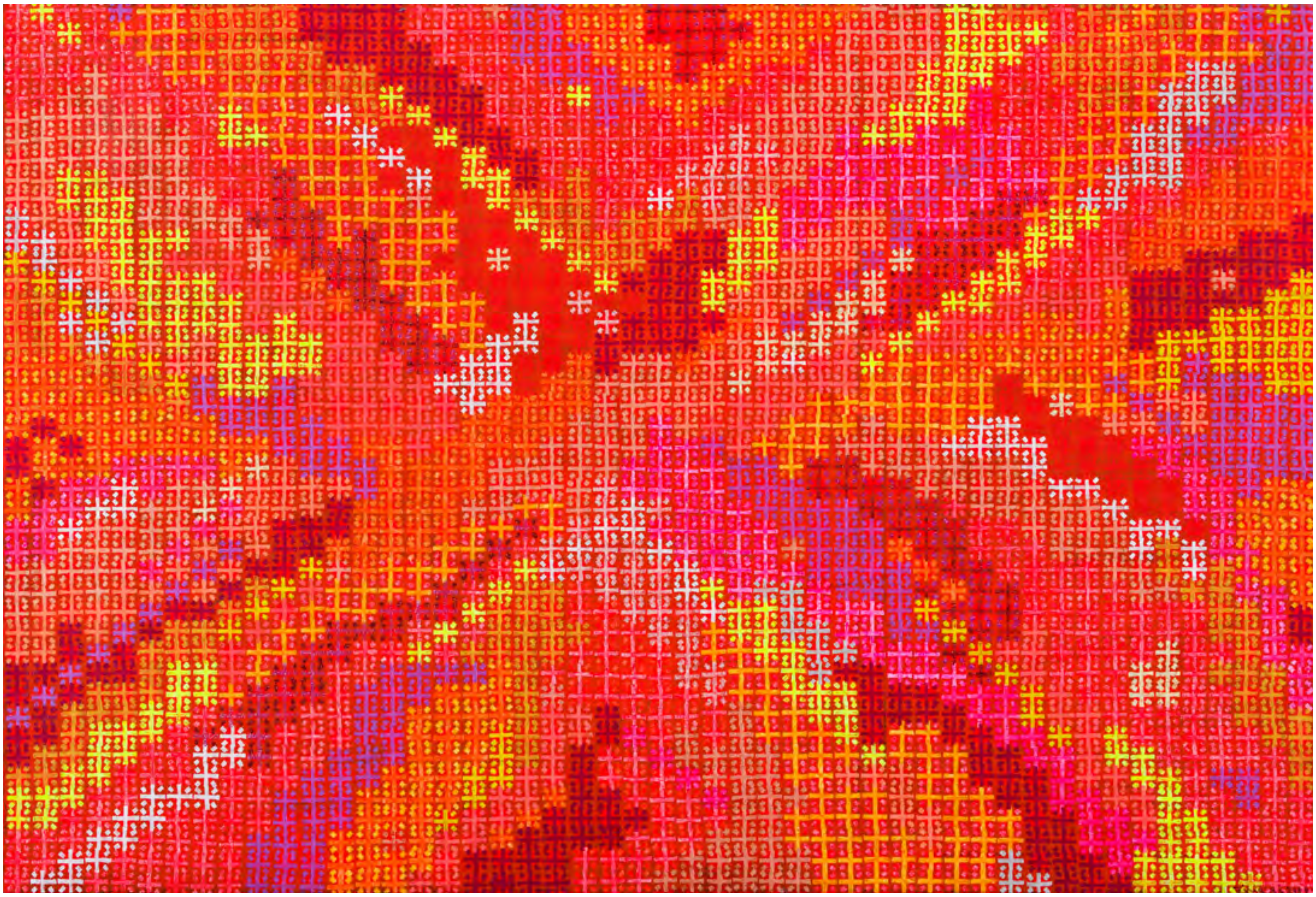
Collecting art has been a keystone activity among successful individuals and families across the globe for centuries. The benefits are manifold and continue for collectors active today. In addition to living with great objects that bring daily enjoyment and curiosity, owning art offers a platform for personal expression, provides a direct tangible connection to the broader creative heritage, and frequently grows into a rich source of intellectual engagement providing many years of fascinating exploration. An art collection may even become a store of value, both financial and cultural, empowering its owners to create a lasting legacy across generations with the works they've assembled. Furthermore, individuals often grow out from their role as private collectors to become stakeholders in the global art ecosystem: influencing trends, shaping markets, and contributing significantly to public-facing institutions and the cultural commons.

The path to building, preserving and activating a collection that fulfills these lofty characteristics is, of course, seldom a clear one. In fact, great collections are recognized as such exactly because so few successfully navigate the many unmarked pitfalls that inevitably arise over the long horizon of being assembled and cared for. This publication aims to make that path a bit clearer for those who strive to build art collections that are meaningful, impactful and structured optimally for long-term value by giving them a practical and sophisticated resource to do so.

Creating a robust art collection over time touches on several overlapping aspects of wealth management, and this publication is a proud collaboration across three relevant areas of expertise at UBS available to our clients: UBS Art Advisory, UBS Family Advisory and Philanthropy Services and UBS Advanced Planning. Viewing collecting through these three related and distinctive lenses, this publication provides an important guide to: (1) navigating the complexities of the art market and managing a collection for lasting value; (2) maximizing the philanthropic impact of a collection; and (3) smartly planning for the intricate tax and strategy considerations inherent in art collecting. Taken together, these essays from their respective areas of subject expertise offer holistic wisdom, insight and advice that collectors may build upon in further partnership with their wealth management team.

UBS has long shown a deep engagement with art and collecting, including our own collection with over 30,000 artworks and our multi-decade sponsorship of Art Basel, among numerous other outlets.
We are as passionate about art and collecting as our clients are. With the resources and expertise reflected in this publication, we bring that commitment to bear directly with our clients in a nuanced, bespoke and sophisticated manner appropriate to the world-class collections they aim to helm. Our goal is for those who partner with us to be recognized as thoughtful, sophisticated and savvy collectors.

Matthew Newton
Director
Art Advisory Specialist
Family Office Solutions



Ding Yi
Appearance of Crosses 2006-3, 2006
Acrylic on tartan
UBS Art Collection

Building an influential collection meant to last

Art Advisory

Situating individual collectors within the global market

According to the Art Basel and UBS Global Art Market Report 2023,[1] the global art market produced sales of $67.8 billion in 2022 between galleries and auction houses—nearly marking a new record and continuing a post-pandemic recovery. That number would likely be even higher if it were possible to track secretive private sales that occur directly among collectors at the top end of the market. The value of art overall has increased over time, and so has the significance and value of sales at the top end of the market. Expensive art is becoming more expensive. This trend follows the increasing concentration of wealth globally. As long as that overall demographic trend continues, the value of art will likely trend with it. Compared to the $100 trillion global equity market, for example, the art market is still quite small. However, even if art collections represent a relatively small percentage of overall wealth portfolios, their collectors place outsize value and meaning on them, frequently spending much of their time and energy acquiring and caring for them.

The United States remains far and away the leader in the global art market, with nearly half of all sales by value occurring here. Within that, New York is still by far the biggest market in the US for art. The United Kingdom and China tend to be roughly tied for second, with France trailing. This points to a world where, while online sales are important and digital marketing is indispensable, being physically present to view artworks remains critical to their transactions. Essentially, people still want to go and look at the art that they will choose to live with—or at least have their representatives do so—and that's easier when the artwork is centrally located. Although most artwork transactions pass through a centralized marketplace in a few major cultural hubs, the artworks themselves end up in the private residences of collectors and public institutions nearly everywhere.

But what does it actually mean to participate in the art market as a family or individual? The bulk of the global art market at the end of the day comes down to very personal decisions made by individuals and families about which artworks they choose to live with—and then what they choose to do with those artworks when it's time to move on. In the global art ecosystem, collectors are not just spectators: they are proactive, influential members driving trends and valuations. Guided by personal taste, professional advice and market knowledge, collectors effectively shape the broader art narrative, contributing significantly to art's cultural and financial value. They don't merely purchase art: they facilitate conversations, alter tastes and define the contours of the global art scene—and they often do this in the context of their families, communities and the broader art world.

[1] Dr. Clare McAndrew, "Art Basel and UBS Global Art Market Report 2023". *theartmarket.artbasel.com*.

Overarching principles and hallmarks of great collections

Successful collectors often find themselves emulating the characteristics of great artists. The spirit of art making is marked by a mix of qualities including individualism, intellectual rigor, taking exceptional calculated risk, decisiveness, obsessiveness, and honing craft and expertise over a long horizon. Meaningful collections are frequently built by individuals who develop similar traits. Often these very same characteristics define leaders in business and successful entrepreneurs. It is common for the unorthodox intellectual worlds of artists to attract those who find success in business and bring their acumen to bear as they begin acquiring works and building collections.

Yet it is no easy task navigating the art market to build a collection that will be personally meaningful, have the best chance at long-term value, remain relevant over time and allow a collector to create cultural impact later if they choose. Collections that meet those standards tend to be guided by a set of principles and hallmarks that set them apart from others.

They are personal and passion-led
Great collections, at their core, represent the individual collector's intimate relationship with the art—mirroring their passions, interests and experiences—often becoming portraits of the collectors who put them together. Frequently, those who are new to collecting want to know what are the "right" artworks to acquire. But leading collections are not merely assemblages of popular or valuable pieces: they are heartfelt expressions of the collector's unique aesthetic sensibility and personal narrative. They reflect the collector's fervor for specific artists, movements, themes or periods, making the collection an outward manifestation of an inward passion and personal honesty uncovered over time. Such collections, being a labor of love, often bring attention to underappreciated artists, overlooked genres or emerging trends, thereby influencing broader dialogues within the art community and directing the interest of others. This personal and passion-led approach grants the collection a unique identity, imbues it with intellectual depth and fosters a level of authenticity.

A collector's love for their works is not only the most rewarding aspect but also a protective shield against changing opinion and market dynamics. Simply put, you need to love it because you might end up as the only one who does. The art world, possibly even more than the financial markets, is susceptible to significant fluctuations and trends. As such, and contrary to popular sentiment, the value assigned to artworks can be unpredictable and often goes down. Even if an artwork retains its historical value, it may still lose market value. Many artworks may remain recognized as important contributions to the history of art, but still not be adopted as valuable by the market.

> Simply put, you need to love it because you might end up as the only one who does.

They are based on a standard of quality
Great art collections, irrespective of their focus or size, are anchored by a standard of quality. Setting that standard crucially helps collectors exercise patience and discernment, and often compels them to pass on a work that doesn't meet their criteria, or to wait, sometimes for years, to acquire one that does. Upholding a standard of quality keeps a collection from being diluted by insignificant or poor examples of an artist's work. It also fosters respect and credibility within the art community, positioning the collection and the collector as significant contributors to the art world. Setting that standard helps ensure that a collection is not only personal but also has the best chance of resonating with a broader audience and the market.

They grow out of expertise
Successful collectors, over time, develop a nuanced understanding of their chosen artworks, artists, their historical context and market backdrop. This expertise and that of their advisors informs acquisition choices, enabling them to separate significant from insignificant works while navigating the complex dynamics of the art market. In many cases, collectors themselves become as informed about an artist's work as professional participants and curators, targeting very specific moments in an artist's career or within a wider movement. In fact, the knowledge of and relationships with artists that many collectors develop become important resources for future scholarship and valuation. Such collectors set the standard for conversation around their chosen areas of focus and the collections may even become more valuable through association with the individuals who built them.

> Collectors are not merely following the market but actively participating.

Their collectors are decisive and take risks
Great collectors tend to be decisive risk-takers. Collectible artworks of quality and rarity are often difficult to find and there may be few opportunities to acquire them. At times, collectors must make swift decisions to secure coveted pieces ahead of their peers. This decisiveness is underpinned by a willingness to take risks. They are willing to focus on works even when they may not align with prevailing trends. Many successful collectors venture into unusual modes of artmaking or ideas and support emerging artists or underappreciated genres, seeing their potential significance and influencing their reception directly. They are not merely following the market but actively participating in its evolution. This combination of decisiveness and risk-taking, backed by passion and expertise, help drive a collection to be an exciting representation of artistic discoveries and personal exploration.

They are built in the context of relationships and a wider community
Art collecting, while intrinsically personal, is far from a solitary endeavor. Great collections are often the result of collaborative efforts, fostered across a broad ecosystem of relationships. This interplay of voices across the art world and elsewhere shapes the collection in a multifaceted and informed manner. Family members, with their shared history and values, often influence the collection's direction and spirit. Curators and historians bring their scholarly perspectives, aiding in contextualizing works and identifying historically significant pieces. Market participants such as dealers and auction house representatives provide insights into market trends and opportunities, while advisors offer guidance on strategic acquisitions and collection management. Engagement with museums can facilitate access to a broader artistic narrative and foster a sense of public responsibility. Other collectors serve as a source of camaraderie, competition and inspiration, enriching the collecting journey. Artists, the creators at the heart of it all, offer the most intimate connection to the artwork, and their input can significantly influence collection-building. This collaborative process creates an intellectual community of trusted relationships: a shared space where ideas, critiques and insights flow freely, refining the collector's approach and vision.

They are part of a cultural heritage and their owners plan for the transition of that responsibility
Building a collection is, in part, an act of cultural preservation and an investment in future generations. Such collections often come to embody a slice of our shared cultural heritage, opening a window to the artistic dialogue, cultural narratives and aesthetic explorations of the time they represent. They become a physical manifestation of a collective memory, preserving artistic milestones for future generations to appreciate, learn from and be inspired by. Collectors who see themselves in that role often take on the stewardship of their collections with a serious and long-term perspective.

They view their collections not just as personal assets, but as cultural treasures whose preservation and transition require careful planning. This may involve the establishment of private museums, gifts to public institutions, succession plans to ensure that a collection remains intact and accessible, or guidance to make sure a collection is sold to best benefit the collector and their interests. Thoughtful planning allows collectors to not only create a personal legacy but also contribute to the continuity and evolution of a shared heritage.

The types of collections that last

Art collections, much like the individuals who build them, are incredibly diverse, reflecting the myriad interests, passions and strategies that fuel their pursuit. There is no one way to build a collection and there are no set categories, but many successful collections fall into a handful of distinctive types. Some collectors are comfortable in the broad sweep of encyclopedic collections, pursuing works across any time period or location while others find fulfillment in the depth and rigor of tightly focused collections. Missional collections embody a collector's commitment to a specific cause or vision, whereas collections centered around emerging artists reflect a penchant for discovery and risk-taking. Multigenerational collections capture the enduring legacy of a family, and some collections cross boundaries between artworks and other rare collectibles such as automobiles, wines or watches. Each category represents a distinct approach to collection building, defined by unique objectives, methodologies and outcomes. Together, they form a broad spectrum of strategies that successful collectors utilize to create collections that are not only personally fulfilling but also stand the test of time.

Encyclopedic or object-specific
Encyclopedic art collections are defined by their broad and comprehensive scope. They usually ignore narrow confines of periods, styles or themes. An encyclopedic collection could span millennia, encompassing everything from ancient artifacts to contemporary works, or it could cover a wide spectrum of a specific type of art or object. The objective is to provide an overarching view, a sort of visual encyclopedia, of an entire field of artistic endeavor. Frequently collectors who are drawn to this type of collection start off pursuing individual objects that they find fascinating no matter how they relate to a greater context. Then, their collected objects grow out from those nodes of fascination.

Encyclopedic collectors often possess a deep-seated curiosity and love for historical knowledge. They typically voraciously acquire, and their appetites are best situated in strategic, far-sighted plans that often grow to include private institutions or foundations. Establishing such collections demands a substantial commitment of time, resources and expertise and frequently grow to include a dedicated curator and other staff members to manage the accumulation of works. Despite the complexities, these collectors find immense fulfillment in the act of piecing together holistic, sprawling collections of rare items.

Focused and in-depth

While the encyclopedic collection is vast and wide-ranging, a focused collection offers a more refined lens into a slice of the art world. This type of collection is characterized by its emphasis on a specific artist, period, movement, theme or medium, providing a deep dive into its chosen subject matter. It's about depth over breadth, with each piece acting as a node within a closely connected network of artworks. If focused on one artist or period, it will often include recognizable major examples alongside minor outlying works that expand the understanding of that area. Creating a focused collection requires discernment, a wealth of specialized knowledge and often a certain level of obsession.

Collectors in this category research, study and seek out the artworks that best represent or challenge the established notions of their chosen domain. They tend to be deeply passionate, persistent and intellectually curious about their chosen focus and enjoy exploring a single topic from multiple angles. These collectors are typically patient, understanding that building a comprehensive and significant focused collection is a marathon, not a sprint. The reward for their diligence is a collection that contributes to a broader understanding of the selected field within the art world. These collections frequently become foundations for exhibitions, scholarship or even the core holdings of museums, ultimately serving as invaluable references for art historians, curators, students and other collectors.

Missional

Missional or purpose-based art collections occupy a unique niche among the various types of art collections. These collections are characterized by a lens of purpose that directs the collector to acquire certain artworks over others. This mission could encompass a range of social, cultural, educational or charitable causes, with the collected works reflecting or advancing these objectives. Artworks in a missional collection can be remarkably diverse, depending on the guiding intent. A collection with a mission of promoting underrepresented artists, for instance, may include works from diverse cultures, ethnicities, genders or socioeconomic backgrounds.

Collectors who build missional collections typically have a passion that extends beyond art. They see their collection as a means of making an impact, of using art as a vehicle to express, highlight or advance their mission. Such collectors in recent years have dramatically altered the market for certain artworks and helped lead to entire new understandings of art in historical periods. Often, these collectors are deeply engaged with their cause, leveraging their influence and resources not just to build a collection but also to foster awareness, provoke thought and effect change in their chosen domain.

> Creating a focused collection requires discernment, a wealth of specialized knowledge and often a certain level of obsession.

Sarah Morris
UBS Wall Painting, 2001/2019
Household gloss paint on wall
UBS Art Collection

Photo credit: Tom Powel Imaging

Emerging artists

Collections focused on emerging artists are a vibrant and dynamic category of art collection. They primarily include artists who are in the early stages of their careers, or late-career artists who have not received widespread recognition. Building a collection of emerging artists is a distinctive endeavor. It requires an adventurous spirit, a willingness to take risks and a keen eye for unrecognized potential. It often involves immersing oneself in local art scenes, visiting graduate shows, staying in tune with artist-led spaces and maintaining relationships with galleries that support rising talent. The process can be exciting and rewarding, offering the collector the thrill of discovery and the chance to support artists at a crucial stage in their careers.

Collectors who focus on emerging artists enjoy the role of being early supporters, patrons who can make a significant difference in an artist's career, sometimes even acting as mentors. They understand that investing in emerging artists carries risk—not every artist's work will appreciate or even maintain its value—but the potential rewards, both in terms of valuation and the satisfaction of having nurtured young talent, can be significant. These collections offer a lively snapshot of the contemporary art world, reflecting current artistic practices and preoccupations. And, sometimes, they mature into significant landmarks of an era's cultural production, acquired affordably in the messy heat of its creation.

Multigenerational

Multigenerational art collections are often a testament to the aesthetic sensibilities, intellectual interests and enduring heritage of a family. They span generations, with each adding their layer of influence and care, and in the process crafting a family legacy through art. Artworks in multigenerational collections might begin with old masters, expand into impressionist pieces in the next generation, and later embrace contemporary works. Such a collection could provide a living record of artistic evolution and a family's interaction with the changing art landscape over time. Or families may choose to honor the tradition of the original collection and preserve it intact from the beginning. Building and maintaining a multigenerational collection demands careful stewardship. It requires not just the acquisition of significant works, but also ownership strategies best suited for the family, long-term preservation of the artworks, and, occasionally, judicious deaccessioning. Families often engage advisors and planners to ensure the collection's integrity, especially during transitional moments across generations.

> Collections of emerging artists sometimes mature into significant landmarks of an era's cultural production.

The collectors who maintain multigenerational collections are typically inheritors of a family legacy, which can be both a point of pride and significant complexity. They are custodians, charged with the responsibility of maintaining and eventually passing on the family's art heritage to the next generation, which is neither easy nor inexpensive. For these inheritors and their family offices, the collection may carry significant market value that can be strategically leveraged and historical value that could be used for social and philanthropic impact. Of course, without proper guidance and care a collection can also become an albatross, occupying a great deal of a family's time and resources.

Cross-collectible

Cross-collectible collections span not just fine art but also an array of rare and highly valued collectible items, from vintage automobiles, high-grade watches and antique furniture, to rare books, fine wine and more. Each of these collectibles carries its own considerations and complexities, which often differ from fine art because they are manufactured in multiples or can be consumed. The unifying thread is not the medium or period, but the collector's desire to accumulate objects of special quality, rarity and aesthetic or historical significance. This form of collecting often involves cultivating relationships with a diverse network of dealers, auction houses and other collectors, as well as frequent engagement with experts across various fields. Collectors in this field typically have expansive tastes, an appreciation for craftsmanship and a passion for history and heritage. They enjoy the thrill of the hunt and the satisfaction of acquiring and preserving rare, significant items. Their collection is a testament to their wide-ranging curiosity, their appreciation for the finest things in life and their commitment to preserving a diverse range of cultural and historical artifacts.

Where to begin?

Beginning to acquire and collect artwork can be exciting yet overwhelming. If you are a novice collector or curious to approach the art world, you may find yourself daunted by the famously opaque and unregulated art market, and you likely have myriad questions about how and where to begin. This section aims to guide you through the initial steps to help demystify the early stages of a collection. From discovering your collecting passion and identifying quality artworks, to determining an appropriate budget and navigating the inevitable missteps, there are certain valuable insights that a new collector can use as guideposts.

Finding your collecting passion
Which art do I like? The important first step of discovering art that resonates with you and that you want to live with is often very personal and starts with exposure and exploration. The best way forward is to view as many artworks as you can. Attend art shows, gallery openings and auctions. Visit museums and art fairs. You may be able to join a network of other collectors that could offer access to private collections and exclusive exhibitions. As you immerse yourself in the art world, observe your own reactions and allow yourself to be honest about which works you find interesting and which you do not. The art world is large with many different potential areas of focus. What types of artworks draw you in? What mediums, styles, periods or themes resonate with you? Do you find yourself intrigued by the intricate stories of old masters; or does the thought-provoking nature of contemporary art captivate you? Perhaps you're drawn to the vibrant energy of Pop Art, or the serene elegance of Asian antiquities?

Remember, there's no right or wrong answer here—only what remains compelling to you. Allow yourself to forget works and pay attention to which works stay top of mind after weeks or months have passed. As your experience and knowledge grow, so too will your understanding of your own aesthetic inclinations and collecting interests. Your passion may be kindled by a particular artist, style, place or medium, or it may evolve out of your own intellectual interests and personal experiences. The goal is to filter down the wide array of collectible art to those objects that genuinely inspire you; those you would love to live with and continue to learn about.

> Allow yourself to be honest about which works you find interesting and which you do not.

Collecting narrowly versus broadly when beginning
When beginning, many new collectors face the decision of whether to follow their instincts wherever they lead across the broad array of art or to quickly focus on a particular area. The choice often depends on a combination of personal interests, financial considerations and collecting goals. If you find yourself captivated by a wide array of artistic styles, periods or mediums, then collecting broadly may offer the most rewarding path. This approach allows for an eclectic collection, provides a wide learning curve and may also offer greater flexibility in terms of market trends. However, it could require a considerable investment of time and resources to develop expertise across multiple areas.

On the other hand, focusing on a specific area can lead to a more coherent and potentially influential collection. If you find a particular style, period or artist that genuinely excites you, then a focused approach may be more appropriate. You may also set a budget that will focus your collection, or aspire to make a significant impact in a niche of the art world. Setting those boundaries can be useful to prevent impulse buying and to ensure your collection maintains a sense of unity and purpose. However, it's also important to allow for a degree of flexibility. One of the joys of collecting art is the opportunity for discovery and evolution. Your tastes and interests will likely develop over time, and it's important to allow your collection the space to reflect this whichever way you choose to engage the vast and varied art world.

Identifying good artworks
Those new to collecting frequently ask how to identify a "good" artwork. Predictably, that is a debatable idea to start with, but most art world participants would acknowledge some art is better than others. Identifying those works involves a confluence of factors, and can be both subjective and objective. The quality of the artwork, the reputation of the artist, the work's provenance and its condition are all critical considerations. Equally important is the artwork's significance within the artist's oeuvre, its historical context and its potential for enduring cultural value.

The art collecting community often considers historical value—how important a work is in the context of art history or within the artist's body of work. This significance can be due to the work's innovative approach, its influence on other artists, its role in a movement or its reflection of the zeitgeist at the time of its creation. Market value, on the other hand, can be influenced by factors like the artist's current popularity, the artwork's rarity, its ownership history or recent sales of similar works. Historical or curatorial value and market value can sometimes align: a seminal work by a renowned artist is likely to command a high price in the market. However, these two values can also diverge. A work may have high historical value due to its cultural significance, yet may not catch the interest of the market for various reasons, including: lack of representation, challenging subject matter, difficulty in preservation or even simple lack of popularity. Conversely, a work might fetch a high price due to a temporary market trend or hype around the artist, despite having less historical significance.

Artworks that have the best chance of being meaningful over time typically exhibit a combination of artistic quality (however subjective), experimentation, historical significance, relevance to wider cultural conversations and likelihood to influence future artistic output. Developing an eye for such works almost always comes with accumulated experience, knowledge and sometimes the guidance of trusted advisors and peers. Understanding these nuances equips a collector with the confidence to separate works of quality that will remain relevant and interesting over time.

How much to spend?

Setting a budget for an art collection can be an important step that many collectors neglect in the beginning. Similar to setting a standard of quality, setting a budget, often allocated periodically, helps collectors to focus and avoid chasing the market. In fact, a realistic budget forces conversations around valuation and may even lead to allocating a larger percentage toward major acquisitions, rather than a multitude of minor purchases. When it comes to how much a collector should spend on an individual artwork, there are no definitive rules. Art and its valuation are of course incredibly diverse, and prices range from a few thousand dollars for a piece by an emerging artist to tens of millions for a masterpiece by a renowned figure. However, a widely used approach among successful collectors is to buy the best quality works that one can afford as quality tends to hold its value over time.

Investing in the best examples of an artist's work doesn't always mean buying the most expensive. It means acquiring pieces that are most representative of that artist or artistic period, and those that are without condition issues or provenance doubts. In this regard, engaging with art advisors, galleries and experienced collectors can provide invaluable insights into assessing quality and understanding the valuation differences between a major work and a lesser or questionable one. Lastly, remember that the budget should also account for additional costs beyond the purchase price, such as insurance, shipping and storage, conservation, framing and possible tax implications. The guidance of an experienced art advisor can be instrumental in navigating these considerations.

Making a mistake
When beginning as a collector, it's important to understand that not every acquisition will fit seamlessly into the evolving narrative of your collection. The path to a great, deliberate and purposeful collection often begins healthily with impulse and meandering exploration, and, yes, occasionally includes purchases that, in retrospect, may seem like mistakes. Mistakes in collecting art are not just common—they're almost a rite of passage. It could be that a piece feels immature as your tastes develop, or you didn't recognize a condition problem in the piece, or its value didn't appreciate as you'd hoped, or perhaps your focus simply shifted over time. Unfortunately, in the unregulated art market, there are even bad actors who deliberately overcharge or misrepresent the works they offer and unsuspecting collectors, even experienced ones, sometimes get caught up in their deals. Yet, these "errors" can serve as invaluable lessons that hone your understanding of your own goals and the art market. Some collectors even choose to keep them as markers of their progress.

To pivot away from such purchases, understand what led you to the decision, reassess it against your evolving collection strategy and use this insight to inform future acquisitions. If an artwork no longer fits your collection, consider selling or gifting it. This allows you to reallocate resources toward works that better align with your collection's direction. Remember, even the most seasoned collectors make mistakes along the way—it's part of the process. The key is to retain focus and excitement about the overall direction, using these experiences to grow and refine your abilities as a market participant.

Keeping the future in mind from the beginning
As you begin acquiring artworks, it's not necessary to have a fixed destination, but it can help to ponder the future. Just as an artist may not know the final form their painting will take when they first put brush to canvas, a collector normally begins accumulating works without a precise idea of their destination—or even a real sense of why they've started. However, the process is often enriched by some forethought into potential future scenarios. Perhaps you envision your collection residing in a museum, or you imagine loaning pieces for exhibitions that create cultural impact. Or maybe your aspiration is to one day establish a foundation or a private museum to display your collection. A desire to create cultural impact, for instance, may lead you to gravitate toward pieces that spur conversation, challenge societal norms or highlight underrepresented artists or themes.

Keeping the future in mind also helps cultivate relationships that can enrich your collection. For instance, if you anticipate donating your collection or part of it to a museum, fostering relationships with museum curators and directors early on can be valuable. If you are interested in supporting contemporary art and emerging artists, connecting with art school faculty and students can provide early access to rising talents as well as inspiring ways that you may support the program through your collection later. Also, developing meaningful relationships with reputable dealers whose interests align with your own can lead to both future acquisition opportunities and open avenues for future sales, if needed.

> A collector normally begins accumulating works without a precise idea of their destination—or even a real sense of why they've started.

These considerations are not about restricting your collection, but about adding another layer of depth and intention. While the joy of collecting is often rooted in the present—discovering artists, attending shows, engaging with artworks—your collection may also become a legacy and considering the future improves the present.

An overview of the art market and its participants

Who are the main players in the art market and what are their goals? The art market is a complex and diverse ecosystem composed of various participants, each with distinct roles, motivations and aspirations. This eclectic blend includes galleries and dealers, auction houses, museums and their curators, art fairs, independent advisors and service providers, fellow collectors, and, of course, the artists themselves. Each participant is a unique part of the market's dynamic interplay; however, their roles are not isolated: there is a significant overlap in the ecosystem of the art world and very often individuals move between these roles. For instance, galleries and auction houses work closely with independent advisors and collectors, and artists might collaborate directly with museums or curators. Many of the service providers in the art world are also working artists. Some collectors who actively buy and sell become professional art dealers themselves. The interaction among these players ultimately fuels the art market, shaping trends, values and the direction of artistic discourse.

For a collector, understanding the motivations and goals of these different players is fundamental. It equips collectors to better navigate the art world, collaborate effectively, position themselves to optimize their collection and even help to avoid back dealing among insiders. This understanding can also inform the creation of strategic relationships that benefit both the collector and their partners in the art world. By gaining insight into the art market participants' distinct roles and shared interests, a collector can leverage this knowledge to curate a collection that aligns with their vision, passion and long-term goals.

> There is significant overlap among roles in the ecosystem of the art world and individuals often move between them.

Galleries
Galleries and dealers are pivotal participants in the art market ecosystem with the primary goal of promoting and selling artworks. Contemporary galleries, often synonymous with primary market dealers, focus on representing living artists. They nurture artists' careers, manage their exhibitions, promote their works and sell their latest creations directly to collectors. Galleries are usually the first point of contact for collectors looking to acquire pieces from emerging or mid-career artists. Primary galleries typically consign artworks from their artists rather than maintain an inventory that they own outright. In a typical arrangement, the gallery carries costs associated with the exhibition, storage, care and marketing of the artworks and any amount from sales are divided equally between gallery and artist.

Secondary market dealers, on the other hand, specialize in buying and selling artworks that have been previously owned—hence the term "secondary." They often deal with art from deceased artists or their estates, historical pieces and works resold from private collections. Their role is to find buyers for these previously owned works, which sometimes include highly sought-after pieces that transact privately with the gallerist acting as broker. Often gallerists who begin in the primary market grow into coordinating profitable secondary market deals as they develop a network of clients with common interests.

The motivations of galleries and dealers revolve around promoting their represented artists, selling artworks and maintaining a strong network of collectors and institutions. They seek to cultivate relationships with collectors and institutions who will appreciate, care for, and ideally keep the purchased artworks long term, and they normally want the opportunity to resell valuable works in the future back through their network, earning a commission.

Successful collectors frequently build trust-based relationships with reputable galleries and dealers; this can lead to preferential access to sought-after pieces and valuable advice on acquisitions. To navigate these relationships effectively, it helps for collectors to understand their own interests and tastes, communicate them clearly and develop commitment to the artists and artworks they choose to support.

Auction houses

Auctions are an integral clearing house and source of price discovery in the art market, serving as a dynamic platform where collectors, dealers and institutions buy and sell artworks of almost all types. Auction houses handle a variety of transactions, including sales of individual works, entire collections and estates. Some of the most high-profile transactions in the art world happen under the hammer, with artworks often achieving record prices. Auction houses also frequently offer estimates of artworks' market value, both to assist collectors who need appraisals and to help them source consignments for the auction house from collectors.

An auction house's lifeblood is consigned artworks and their primary goal is to maximize the value of the items sold, which in turn maximizes their commission. This is typically achieved by creating a competitive bidding environment and expertly marketing the artworks to potential buyers. Auction specialists—often experts in specific categories of art—play a key role in this process. They seek out consignments, curate the artworks for sale, determine their estimates and gauge interest in the market for the upcoming lots.

Navigating relationships with auction houses requires a keen understanding of their role and motivations. Auctions are the most transactional element of the art world, which can aid collectors if engaged thoughtfully or can sometimes leave a collector disappointed if not. Collectors should remain aware that auction houses represent the seller's interests and their goal is to achieve the highest possible sale price. Building a relationship with a trusted auction specialist can prove helpful, providing access to a wealth of market knowledge and advance notice of upcoming lots of interest. Additionally, collectors should educate themselves on the auction process, whether they are buying or selling, including understanding buyer's premiums and other fees, conditions of sale, reserves, guarantees, marketing and the intricacies of bidding, to ensure they make informed decisions, understanding that most of these points are negotiable.

Museums

Museums, of course, play an indispensable role in the art world as custodians of our shared culture and history. Museum curators, with their deep expertise and commitment to cultural preservation, are responsible for acquiring, managing and presenting artworks in a manner that respects their historical and cultural significance—and they frequently are also important relationships for collectors. Curators are driven primarily by the desire to enrich the public's engagement with art and its cultural narratives, but they also need meaningful and supportive relationships with prominent private collectors. Their acquisitions and exhibition choices, sometimes supported by or even sourced from private collections, can have a profound influence on an artist's career and market value. At varying times, museums may be either competitors or partners with collectors for acquisitions. An artist's inclusion in a museum collection or exhibition often signals a validation of their work's significance, which can increase demand and market values. However, collectors should be mindful that while museum exhibitions often enhance an artist's reputation, the commercial success of an artist's work remains subject to many other market dynamics.

The relationship between galleries and museums is complex and often symbiotic. Galleries rely on museums to provide their artists with critical exposure and credibility, while museums often rely on galleries for their commercial expertise, access to artists and, sometimes, financial support. It is not uncommon for curators at museums to work simultaneously as private art advisors to local collectors or later take sales roles at commercial galleries or client development work at auction houses.

For collectors, building relationships with museums can provide access to a wealth of knowledge about historical context, artistic movements and emerging trends. It can also open doors to philanthropic opportunities, such as lending or gifting artworks, supporting exhibitions or contributing to acquisition funds. Private collectors often play a crucial role in the management and governance of museums by joining or even leading museum boards. As board members, they help guide the strategic direction of the institution, drawing from their own experience and passion for art to support the museum's mission.

The responsibilities of board membership are significant, including financial commitments, fundraising, budget oversight and policymaking. Time is another major consideration. Board members typically attend regular meetings and participate in various committees. They may also be asked to represent the museum at exhibitions, openings and other public events. Navigating the politics of a museum board can be a delicate task. Each board has its own culture, and board members must often balance differing opinions and competing interests. Yet there are many rewards from serving on a board. Membership often offers unique opportunities to contribute to the museum's programming, through both acquisitions and loans, and to foster important relationships with curators, artists and other collectors. These engagements not only expand a collector's influence and network in the art world, but also provide a fulfilling avenue for giving back to the community and advancing the public's understanding and appreciation of art.

Art fairs

Art fairs today are a pivotal exchange place in the global art market, serving as key platforms for galleries to showcase and sell their artists' works to a diverse and international audience. They have grown significantly in the past decades, becoming critical sources of revenue for some participating galleries. From Art Basel, spread across three continents, to specialized fairs focusing on specific periods, regions or mediums, art fairs now punctuate the annual calendar in many of the world's major cultural hubs. The business model of art fairs revolves around galleries applying for entry and then paying for exhibition space. Fair organizers select galleries based on various factors, including the quality of their programs, their history and how their offerings align with the fair's focus. Once admitted, galleries present a curated selection of artworks, aiming to capture the attention of wealthy collectors, curators, critics and art enthusiasts.

Sales at these events can significantly impact a gallery's annual turnover, especially at top-tier fairs where high-profile collectors come prepared to make significant acquisitions. Beyond transactions, art fairs also provide a critical networking platform. They allow galleries to foster relationships with existing clients and to meet potential new collectors, deepening their engagement with the global art community. Similarly, collectors can use the opportunity not only to acquire works, but to network with like-minded peers, participate in auxiliary social events and glean important market insights directly from its participants who have all gathered in one area.

Collectors
Other collectors can provide an interesting tapestry of insights and perspectives as a collection is assembled. Like-minded peers offer both inspiration and validation, presenting different angles of approach, nuances of taste and sometimes a friendly competition that can spur a collector's ambition. Networking and establishing relationships with other collectors often leads to fascinating conversations and discoveries about artists, genres and specific works. These connections can create a sense of community, foster the sharing of experiences, and even provide opportunities for joint purchases or trades that wouldn't be possible alone. However, navigating relationships with fellow collectors also presents certain challenges. As collectors are sometimes competitors for scarce resources—particularly for highly sought-after works or emerging artists—it's important to maintain a level of discretion and respect for each other's pursuits. There is a delicate balance to maintain between collaboration and competition, openness and discretion in those cases. The art world is still very much a relationship business and collaboration among collecting peers can create a powerful resource of shared information.

> Collaboration among collecting peers can create a powerful resource of shared information.

Artists
Artists work at the nucleus of the art world. They are the originators, the creators and the very heartbeat of the ecosystem, providing the content around which the entire industry and market revolves. What motivates them varies widely: self-expression, the desire to communicate or provoke, the need to explore and challenge artistic or societal boundaries, or a combination of these and more. Some actively engage the "art world" while others recoil from it. Some become celebrated household names while most others—even when recognized and influential within the art world—remain relatively obscure outside of it.

Understanding and appreciating an artist's work involves learning what motivates them, their techniques and their personal journeys. In other cases, though, artists prefer that their work "speak for itself" and they choose to share little about their process. A deep and genuine interest in these nuances not only enriches the experience of collecting but also allows artists to trust their collectors. Very often, many collectors cite their friendships with artists as one of the most rewarding aspects of collecting.

Artists can be approached directly in some cases, particularly those who are emerging or mid-career, or through the galleries that represent them. When engaging with artists, collectors should remember to respect their creative process and autonomy. It's also crucial to approach interactions with artists with a sense of partnership. You're not just buying their work; you're often supporting their career, endorsing their vision and even becoming part of their extended artistic community.

Some collectors pursue buying art directly from artists, especially emerging artists. However, buying directly from artists also carries certain risks and considerations. Removing galleries from the equation can place both parties in unfamiliar territory, potentially leading to misunderstandings around valuation or the handling of the transaction. Galleries often provide a structured framework and help to stabilize the market for some artists. Moreover, buying directly can affect an artist's relationship with their representing gallery, which is often an essential support structure for many artists. For this reason, it's often recommended that collectors maintain open and respectful communication with both the artist and any representing galleries, aiming for a transparent and mutually beneficial transaction when the opportunity occurs.

Service providers
In the context of collection management, we will outline the important roles that various service providers fulfil in the art market ecosystem and when it is best for collectors to engage them.

Transacting in the art market

Collections are most often built, of course, through purchases. Choosing which artworks to acquire is the important starting point, but completing the transaction successfully and in a way that protects the collector is the crucial next step that often doesn't receive appropriate attention. Transactions in the art market can be opaque and are even sometimes treated without thorough scrutiny by many market participants considering the valuations involved. Collectors also face questions on what influences the pricing of artworks, how to properly conduct due diligence on potential acquisitions, and how to choose trustworthy partners for transactions. Further, it's often important for collectors to consider the common legal structures used for art transactions.

The pricing of art

In the art market, determining the price of an artwork is a complex process influenced by various factors. This is largely because artworks aren't commodities with clearly defined value parameters but are unique, often emotionally charged items. Prices are initially set by the primary market, which includes artists and galleries. They consider factors like the artist's career trajectory, demand for their work, exhibition history, and the size, medium or subject matter of the piece. Secondary market prices, set during public auctions and by secondary dealers, rely heavily on the artwork's previous sale prices and the current market demand. Being unique objects, in some cases their owners assess a price that is completely unrelated to the wider market and based solely on their willingness, or lack of willingness, to part with the artwork. Or, as often happens, a collector simply would not consider selling a piece at any price.

While there are considerable nuances here, prices can be broadly categorized into low-, middle- and high-end markets. Low-end market artworks typically include works by emerging artists or less-known artists, with prices often in the thousands to tens of thousands. Middle-market artworks generally fall within the tens to hundreds of thousands range and usually include works by mid-career or recognized artists. The high-end market, comprising artworks often valued in the millions, typically involves the best examples by blue-chip artists with international reputations and solid records of high sales. The stability of an artwork's price often relates to its category: high-end artworks usually have more stable prices due to established demand, whereas lower-end artworks might see more price volatility due to fluctuating market trends. That said, valuations for individual artists or genres often decline or grow substantially across all price categories.

Due diligence during artwork transactions

Due diligence during artwork transactions can involve detailed research prior to finalizing a purchase and be a crucial step to safeguarding a collector's investment. A key task is establishing the artwork's provenance, or ownership history, from the time of its creation to the present. Depending on the age and history of an artwork, provenance may be murky. But, making best efforts through expert research to verify the provenance can substantially alter the valuation of an artwork and even confirm or invalidate its legitimacy. Authenticity goes hand-in-hand with provenance and often involves expert opinions or scientific analysis to verify that the artwork was indeed created by the stated artist, especially if there is any doubt. Alongside provenance, it is vital to evaluate the condition of an artwork, typically through a condition report completed by an expert independent conservator that identifies any damage or history of conservation. Examining the artwork's exhibition and publication history provides further context and validation of the piece's value. Determining clear title and ownership is crucial to avoid any potential legal issues down the line, ensuring that the seller has the legal right to sell the piece. The Art Loss Register provides certificates to demonstrate that an artwork is not reported as stolen, lost or subject to a dispute. For some transactions, export documentation might be necessary, depending on the artwork and the countries involved. Lastly, it is important to compare the offered price against similar market valuations when possible, to ensure that the price is not dramatically out of line. Although when collecting artworks there isn't always a direct comparison or there may be few reference points available and an independent assessment may be necessary in which a collector simply asks of themselves whether they're willing to pay the price offered to acquire the work.

Who to work with when purchasing and who to avoid

Navigating the art market requires not only an appreciation of art but also a discerning eye for reputable market participants. In an unregulated market, longevity and a history of transparent transactions are key indicators of trustworthy galleries, dealers and auction houses. They should also demonstrate in-depth knowledge about the artists they represent and the works they sell, offer comprehensive documentation about the artworks, and readily provide references from other collectors or institutions. Art advisors and consultants should hold credentials from recognized industry bodies and have a substantial record of successful work with clients.

On the contrary, be wary of market participants who guarantee that an artwork's value will appreciate or who use value appreciation as a selling point. The art market is highly speculative and no one can accurately predict future prices. Similarly, avoid those who rush transactions, discourage independent appraisals, or are reluctant to provide comprehensive documentation about an artwork or don't welcome third-party conservators, for example. It is also concerning if they cannot easily reference other collectors and institutions who they have ongoing relationships with or if they have not been validated by third-party associations or publications. In the art world, where relationships are paramount, reputation is a crucial barometer for integrity and trustworthiness. Engaging with reputable art market participants is fundamental in building a great collection while ensuring the protection of your acquisitions.

> Artwork transactions can involve detailed research prior to finalizing a purchase.

Structuring purchases of art

The topic of structuring for art collections will be addressed in full in the final section of this publication, but a quick overview is included here for reference in the context of transacting. Art collectors often employ a variety of legal structures to manage and protect their acquisitions. Each structure provides different benefits and potential limitations, influenced by the collector's goals, tax circumstances and estate planning needs. For instance, a private foundation can be established by collectors aiming to give the public access to their collection, or those seeking other philanthropic avenues. However, private foundations are subject to regulation and scrutiny. Limited liability companies (LLCs) provide collectors with privacy and liability protection. They also allow for flexibility in terms of management and may be used when multiple parties, such as those in a multigenerational family, are involved in the ownership and decision-making process of the collection. Trusts offer a robust estate planning solution, allowing a collector to pass the collection onto future generations in a tax-efficient manner. Trusts can protect the collection from potential creditors and facilitate a smooth transition of ownership. It's also important to understand the tax implications associated with these structures. Art is generally considered a collectible under the US tax code, and thus gains from a sale of it may be subject to higher maximum capital gains tax rates than gains from the sale of other capital assets. Also, buying, selling or gifting artworks may be a taxable event for income tax, estate tax or sales tax purposes. As always, individual circumstances can vary widely, so it's essential to seek professional advice before establishing any such structure for an art collection.

> Many of the collections that have appreciated most in financial value were built by collectors driven by love for the art itself.

Risks of considering art as an investment

As the values of artworks have risen in recent years and record-breaking sales have made headlines, collectors commonly wonder how to think about art in investment terms. Buying art purely as an investment is fraught with unique challenges that require a high level of understanding and caution. Firstly, the art market is famously illiquid. Unlike more traditional investment products, artworks normally cannot be sold instantly or at a predictable price. Timing is also precarious, as tastes and market preferences can fluctuate dramatically, making it difficult to sell for a profit at a particular moment. Secondly, artworks come with considerable "carry costs." These include insurance, storage, conservation and fees associated with both buying and selling the work. It's important to remember that these costs may accumulate over time, potentially offsetting any gains made from the increase in an artwork's value. Additionally, the art market is notorious for its opacity, especially regarding pricing. Unlike traditional financial markets, there's no real "ticker tape" for the price of a unique object, although some market data is available. Finally, risks related to the title, provenance and condition of artworks can have a considerable impact on their value. Artworks may have a complicated ownership history, potentially leading to disputes over title. Provenance can also throw up surprises, with newly discovered details potentially undermining an artwork's value. Similarly, condition issues can affect an artwork's value and may only become apparent after purchase.

These complexities underline the importance of engaging with the art market out of passion first, and considering any potential financial gain as a secondary, and highly uncertain, bonus. Counterintuitively, many of the collections that have appreciated most in financial value were built by collectors driven by love for the art itself.

Basic resources for professional collection management

A collection built to last requires proper care to ensure it does. Collectors have the responsibility of not only selecting works that remain relevant over time, but also their safekeeping to ensure the collection retains its value and is ready when it is time to consider legacy plans and sales. This is broadly referred to as collection management, which is best executed with a network of trusted service providers in place, each bringing specialized expertise.

Inventory management

Inventory management, registration and the maintenance of accurate records are an important first step in managing an enduring art collection. Often easily overlooked by collectors who are starting out, keeping organized records about each artwork empowers collectors to make smart decisions around their collections. A collection management system tracks essential data such as the artwork's title, artist, year, medium, dimensions, conservation history, provenance, acquisition details and location. This information not only assists with accurate appraisals, insurance claims and legal inquiries, but it can even enhance the artwork's historical and monetary value. Collectors should also consider the practicalities of maintaining the condition of work on view in their private spaces over periods of time, such as light exposure, careful installation and security systems when necessary. For collections at a certain scale, it may even be helpful to employ a registrar, or a dedicated professional who manages these tasks and maintains the coherence and integrity of the inventory. These professionals ensure records are regularly updated, manage the logistics of artwork movements and liaise with various service providers from insurers to appraisers and conservators.

Appraisals

Appraisals are an essential tool for maintaining and managing an art collection, serving multiple purposes depending on the specific needs of the collector. There are several types of appraisal, each used in unique circumstances. Insurance appraisals are performed to establish the replacement cost of an artwork in case of loss or damage, whereas fair market value appraisals are used for tax purposes when considering charitable donations or estate tax assessments. If you plan to sell an artwork, you'll want an assessment of market value that estimates the most likely sale price for the piece.

Independent, professional, certified appraisers should uphold a set of standards in their work that ensures the appraisals are fair, consistent and reliable. These standards are primarily guided by the Uniform Standards of Professional Appraisal Practice (USPAP), which serves as the quality control standards for all appraisals in the United States and its territories.

The frequency of appraisals depends on the volatility of the art market and the nature of the individual artworks. However, a general rule of thumb is to have your collection appraised every three to five years. High-value and rapidly appreciating artworks should be appraised more often to keep up with changes in the market. Regular appraisals are crucial not just for ensuring insurance coverage is adequate, but also for understanding the growth and value of your purchases over time, which may influence strategic decisions with the collections.

Shipping and storage logistics
Proper shipping and storage logistics are important for maintaining an art collection, and these services often require a specialized approach due to the delicate and high-value nature of artworks. Specialized collectible shipping and storage services can be quite costly, especially for large collections or particularly valuable or delicate pieces, but those costs should be weighed against ensuring the longevity and safety of your collection. When shipping, it is important to choose a company experienced in fine art handling that provides bespoke crates, temperature-controlled vehicles and expert installation. They should adhere to best practices in terms of handling and transporting artworks to avoid any damage. For long-term storage, collectors should consider facilities that offer climate-controlled environments, specifically designed to protect artwork and meet stringent security standards to protect against theft and environmental hazards. Some facilities also offer viewing rooms where collectors can privately view their stored art. Storage facilities in certain jurisdictions market themselves as "free ports" in which art delivered there is in a kind of limbo state and may not be subject to sales taxes, use taxes, import taxes or duties until it is removed. This can be a strategic choice for collectors considering long-term storage, international transactions or estate planning strategies. It's essential to consult with an art advisor, attorney and/or tax advisor before deciding to use such facilities, as they can have complex legal and tax implications.

Collectible insurance
Securing proper insurance is a fundamental part of maintaining and preserving a lasting collection. Fine art insurance is distinct from other types of insurance due to the unique nature of the assets it covers, and well-known insurance companies often have fine art and collectible specialists on their teams. Artworks are often irreplaceable, carry significant cultural value and can appreciate over time, making their protection critical. The idiosyncratic risks associated with art, such as high valuations, vulnerability to environmental conditions, transit-related risks and the complexities of valuation, often require specialized coverage.

There are two primary types of fine art insurance policies: itemized coverage, where each piece is individually listed and valued, and blanket coverage, where the entire collection is insured up to a specified total value. The choice between these often depends on the nature and value distribution within a collection. To acquire a fine art insurance policy, collectors typically need to provide detailed information about the artworks, including their condition and value. These details are often provided through professional appraisals. The insurance company may also require information about how and where the artworks are stored and displayed, and any security measures in place.

Furthermore, given the dynamic nature of art collections—growing, changing and sometimes appreciating over time—insurance policies should be reviewed and updated periodically to ensure appropriate coverage. It's highly recommended that collectors engage with insurance brokers or advisors who specialize in fine art, to ensure that their unique needs are adequately met.

Art legal services

Ultra high net worth individuals and families who may have intricate ownership structures and execute complex transactions can benefit from the advice of art legal services. An art lawyer's expertise can span a range of relevant fields, including contract law, intellectual property, tax law, estate planning and international law, each of which can intersect in the realm of art collecting. Art lawyers are sometimes useful when transacting in the art market. They help in drafting and reviewing sales and purchase agreements, which are too often overly simplified by sellers, ensuring that the terms are fair and protect the collector's interests. This could involve, for instance, ensuring the seller provides warranties as to the authenticity and clear title of the artwork. They also advise on the tax implications of buying, selling, donating or inheriting artworks.

In addition, the opinion of art lawyers can be useful when setting up legal structures such as trusts, foundations or LLCs for owning and managing the collection, particularly in the context of estate planning. They can help establish the appropriate legal framework that ensures the collection's preservation and the collector's legacy for future generations. And, of course, art lawyers are key players in resolving disputes that may arise, such as questions of authenticity, provenance, copyright infringement or ownership disputes. Lawyers with both a deep understanding of legal frameworks and the nuances of the art world can be helpful partners in managing and protecting a valuable art collection.

Art advisors

While some collectors enjoy engaging in all aspects of a collection directly and personally, others find that art advisors serve an instrumental role in navigating the intricate, sometimes opaque world of art. Their main role is to provide guidance and advice tailored to a collector's individual tastes, budgeting goals and logistical needs, ranging from acquisition strategies to collection management. For new collectors, advisors educate on art history, the art market and collecting strategies, fostering informed decisions and helping to cultivate individual taste. They guide collectors toward meaningful and impactful acquisitions, making sure purchases align with the broader collection's narrative and purpose. For established collectors, advisors can help to refine and focus a collection, assist in acquiring or selling works, manage collection logistics and provide market analysis. They can also facilitate relationships with galleries, artists and other collectors, offer guidance during art fairs and auctions, and use their extensive networks to access works that might not be publicly available. Art advisors also provide essential expertise in conducting due diligence before a purchase, including inquiries about authenticity, provenance and fair market value. They can assist with the management aspects of a collection too, serving as a nexus for the specialized services described above, such as insurance, storage, shipping and appraisals.

> Contract law, intellectual property, tax law, estate planning and international law can each intersect in the realm of art collecting.

Thoughts on new technologies in art and collecting

The art world is continually evolving, now as much as ever influenced by emerging technologies that are reshaping the landscape of creation, ownership and investment. Let's delve into some of these new developments: non-fungible tokens (NFTs), artificial intelligence (AI) and generative art, and securitized art platforms.

NFTs have stirred considerable buzz in recent years, primarily for their speculative market but also for their potential in validating digital ownership and establishing provenance. While the notion of digital art is far from novel, NFTs may offer a new way to establish and trace an artwork's origin and ownership, which is especially attractive to artists who have grown up digitally native. However, the artistic value of NFTs should not be overstated merely because of their technological novelty; they are best understood as a tool for ownership or membership, not necessarily a genre of art itself.

AI and generative art present a more profound intersection of technology and art. These advancements have introduced an entirely new medium of artistic expression, expanding the boundaries of creativity much like the invention of photography did in the 19th century. As AI and generative techniques permeate into creative practice, they are likely to alter how artists think of using traditional mediums and will lead to unexpected developments in visual language. They may also concurrently amplify the appeal of handcrafted, one-of-a-kind pieces. In an era of mass replication and infinite instant images, the allure of rarity and individualism is enhanced, and such unique artworks may gain heightened interest and value.

Turning to securitized art platforms, a note of caution is necessary. These platforms, which propose art as a fractionally owned investment, have proliferated recently. They offer the opportunity to own a portion of a securitized artwork and participate in its appreciation. However, they are untested by time—a crucial factor in establishing the value and resilience of art. Advertising returns comparable or superior to traditional equity markets, these platforms often obscure the inherent risks and intricacies of the art market. Claims of consistent high returns either reflect a fundamental misunderstanding or oversimplification of the art market's nature or a deliberate attempt to overlook its risks. It's important for collectors to approach these products with a healthy dose of skepticism. As always in the realm of collecting, education, due diligence and a sense of personal passion and enjoyment should guide your steps.

Lending against art as collateral

For some collectors, their valuable art collection offers aesthetic enjoyment and also doubles as a potent financial tool. Lending against art as collateral is a strategic method of accessing a portion of the value of their collection without having to part with the artworks themselves. Collectors might take out loans against their collections for a range of reasons. For some, it's a way of managing cash flow, especially if they're awaiting returns from other investments. For others, it's a way of freeing up capital for further acquisitions, allowing them to seize opportunities in the art market without liquidating assets. Additionally, these loans can serve broader wealth management strategies, enabling collectors to diversify their portfolios, invest in business ventures, manage estate planning or even gift to charitable causes while maintaining ownership of their art.

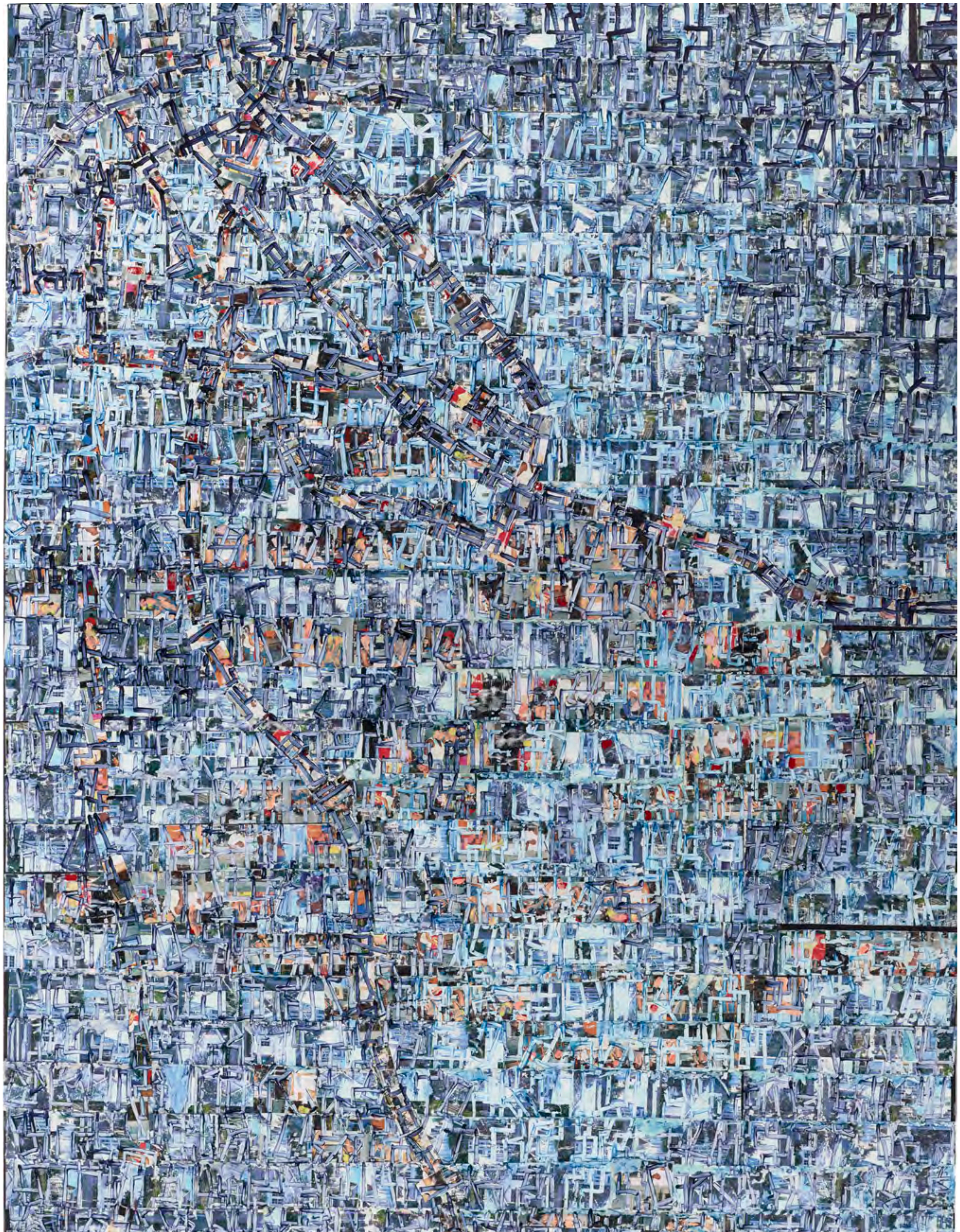
Art loans are typically structured as a line of credit, secured by the artworks themselves. The lender, often a bank or specialty finance company, evaluates the artworks and assigns them a value based on various factors, such as the artist's reputation, the artworks' provenance and condition, and current market trends. The loan-to-value ratio usually ranges around 40% to 50% of the appraised value, though this can vary. Interest rates typically hover around the mid-single digits above the Secured Overnight Financing Rate (SOFR) but can fluctuate depending on the overall credit profile of the borrower and the specifics of the collateral.

While loan sizes can vary dramatically based on the value of the art serving as collateral, loans typically start in the low six or seven figures and can reach into the tens of millions or more. It's essential for collectors to understand that, while potentially beneficial, borrowing against their art does involve risk, and expert financial advice should be sought when considering this strategy. The art world's lack of price transparency and the illiquid nature of the market can make loan repayments challenging if the borrower's financial circumstances change unexpectedly. As with any financial venture, understanding the potential rewards and risks is crucial.

Federico Herrero
Untitled, 2019
Oil and acrylic on canvas
UBS Art Collection

Concluding remarks

Reflecting on this high-level exploration of the multifaceted art market, it is clear that great collections are not built by accident. They are driven by passion, but equally characterized by thoughtful intention, a coherent narrative (even when only seen in hindsight), careful stewardship and a deep connection to the broader art world. It's a journey marked by calculated decisions, an understanding of market dynamics and the right partnerships. The advent of new technologies and market mechanisms will bring both challenges and opportunities, requiring a nuanced understanding and a discerning eye. Looking forward, it will be important and exciting for collectors to consider the philanthropic potential of their collections and the impact they can make in the cultural landscape. Additionally, considering the complex tax and structuring implications associated with art collections will round out a sophisticated collecting plan.



Rick Lowe
Project Row Houses: People and Place, 2021
Acrylic and paper collage on canvas
UBS Art Collection

Parallel passions

Family Advisory and Philanthropy Services

Parallel passions

A love for art can be born organically from a personal experience, or it can be introduced and incorporated as part of a family legacy. It can start with a visceral response to a work of art and burgeon from there, or it can be initiated and informed by those around you (i.e., you hail from a family of art collectors or art lovers). Decision-making around art collecting can take an active or more passive path—one can become a student of art and pursue knowledge that will inform and inspire further collecting, or it can be primarily driven by the responsibility of stewarding a family's strategic acquisition and maintenance plan. Even in the latter example, there is room for incorporating new views, passions and interests in the further evolution of a collection that may already be a multigenerational endeavor.

The multiple paths to becoming a collector and its evolving trajectory can be similar to that of becoming and evolving as a philanthropist. Just as an art collection has an inception point and an intentional direction, philanthropy is inspired by passion and purpose. We often say that "philanthropy is biography." To know what is important to a person, we have a look at what charities or causes they support. This can provide meaningful insight into what they have experienced in their own lives that inspires their giving.

The passion for art can be harnessed to create positive change and a parallel activation can ensue. This section will highlight key ways in which an art collection and a passion for all things art and culture can inspire simultaneous philanthropic pursuits.

Your art on view: owning, loaning and gifting

We often hear the adage that "people give to people." Acquiring, loaning and gifting works of art can be rooted in a similar dynamic—through collaborating and cultivating partnerships around the passion of art.

Getting started: owning
Collecting works of art is often considered a form of self-expression, a deeply personal catalogue of one's beliefs and interests. You may begin collecting works of art you simply like to surround yourself with; your collection may even begin to grow and evolve thematically, and you may become more deliberate about how you begin to acquire. But where do you start? How do you know who are the "right" artists and works of art to collect? How do you find out where to purchase them? To educate yourself about artists and works of art in a specific genre you would like to own, developing a relationship with a fine art museum or gallery is a good first step.

Developing a collection begins first with relationship-building. It can be useful to engage with an art consultant, a museum curator, artists or become part of a collecting circle. If you love a particular museum and its collection, you can learn about its works and, in turn, the museum will nurture its relationship with you as a donor and collector. This mutual relationship may begin with your interest and query for guidance from a specialist, such as a curator or the director of the museum. A potential eventuality could be for works from your own collection to reside within the museum walls and/or be available for public view. In fact, a significant responsibility for museum leadership is to cultivate relationships with those who will be able to gift works of art and/or financially support the purchase of new works of art.

Collecting circles

A collecting circle, a type of giving circle, brings together a group of art enthusiasts who share a passion for art collecting.

They support the growth and development of an organization's (or community's) art collection.

This collaborative group of engaged individuals develops a deeper knowledge of art, shares ideas and fosters personal connections with curators, art consultants, artists and collectors.

Loaning

Navigating loaning your works of art to a museum

It can be flattering and affirming when an arts institution reaches out and asks if you would consider loaning or lending your work of art to its museum or special exhibition. Many times, the curator will have spent years planning and outlining the exhibition and has already identified your piece(s) to include therein. Museum curators learn of works of art that belong to private collections through private sale, from gallery owners, or if they have previously worked to curate a donor's personal collection. Often, the collector has an existing relationship with the organization or inquiring museum.

What to consider when approached to loan a work of art (or a collection) to a museum:

- How would you feel about your work of art being away from you?
- Is the request for a work of art to be part of an exhibition, a traveling exhibition or for a local installation?
- For what length of time is the request and is it for the run of show? Or is this for a permanent loan agreement?
- What type of loan terms would you agree to?

If you decide to move forward, know that the process of loaning a work of art to an organization varies by organization, length of loan, type of art and location. However, there are a few common policies—a loan agreement and insurance are at the top of the list.

Loan agreement guidelines

The loan agreement is a written and signed document established between the collector and the museum, which should outline the terms of the loan, including the length of the loan, insurance coverage, transportation arrangements and any restrictions on the display or handling of the artwork.

There are good practices we encourage collectors to consider in advance of making the decision to loan. First and foremost, ensure the organization is reputable, has a strong history of responsible loans and no past concerns regarding the care and security of the works of art in its possession. You should also confirm that the museum has the appropriate resources to properly handle and secure the artwork. Museum accreditation organizations, such as the American Alliance of Museums, provide verification for institutions that meet these recognized standards of ethics and best practices.

The loan agreement will detail the terms of the loan including: the transport, condition reporting, placement of piece on display and clauses for any damage that will need restoration or conservation. Another consideration is whether the piece can be photographed and how the collection will be credited and recognized. Each loan agreement should be personalized to the collector and the work itself. It should include details regarding participation in an exhibition, provisions for travel and permissions for the rights and reproductions of images in publications. Loaning takes careful planning, consideration of the risks and responsibilities involved and a clearly outlined plan for who is paying the overall expenses related to loaning the work of art.

Collectors should take the time necessary to adequately consider a loan request (and the recipient entity). Your work of art will be displayed in a public forum for many to view, and it could also be included in an accompanying publication. Loaning can raise the profile of the organization displaying it, encourage giving to that organization and promote academic study. Not only does the work of art benefit the museum's program, but having your work of art displayed in a museum is validating to the organization and adds value to the work of art itself.

Loan agreement good guidelines (with a museum):

- **Condition of the artwork**—before you loan, ensure the piece is properly assessed in its current condition. Confirm the museum will provide a condition report upon receipt and disposition of the work of art so that you can verify the condition did not change during transportation.

- **Insurance coverage while on loan**—the museum should have standard insurance coverage to protect against theft, damage or loss. You may want to obtain additional insurance for the duration of the loan for additional coverage against possible unforeseen loss, potential climate concerns and infestation or vandalism.

- **Clear understanding of security protocols and procedures**—ensure that the museum has sufficient security protocols, including cameras and personnel, both during and after public hours.

- **Transportation**—have the transportation and handling of the artwork clearly outlined to ensure that it is safe and secure traveling to and from the museum and be informed of routes, especially if there are multiple and/or international travel destinations.

- **Art handling**—understand the specifics around installation and de-installation of the work. This includes packing requirements, transport details and condition reports.

- **Collector recognition**—consider how the work of art and collector will be identified and acknowledged. This is typically included in exhibition credit lines and remarks, wall labels, publications and in media. An additional consideration regarding recognition has to do with the actual ownership of the work of art: is it owned by an individual, by a private foundation or a trust?

- **Rights and Reproductions**—Museums have standard clauses stipulating the use of images of the original works of art. Ensure you understand these reproduction rights and are in agreement.

- **Communicate with the museum**—engage with the registrar's office, which oversees the handling. Maintain open communication with the museum throughout the loan period to ensure that the costs pertaining to the loan are outlined, that the work has been properly installed, and that there are no issues or concerns after the artwork has been returned.

- **Understanding the risk**—the piece may get damaged, become lost in transfer, be susceptible to theft or bring unwanted attention to the collector. These risk factors reinforce the importance of conducting due diligence on the quality and professional rigor of the curatorial program. These are all valid concerns and it is within your rights to decline a loan request if you are not comfortable loaning the piece (either in general or to a particular organization).

Loaning art to museums

Loaning art to a museum requires careful planning, effective communication, consideration of the risks and responsibilities involved, and robust documentation.

These steps ensure that the artwork is properly cared for and protected during the loan period.

Collecting, owning and loaning works of art share some benefits—personal fulfillment, affirmation and financial gain. They can also present challenges. The financial and human capital cost of maintaining your collection can be substantial. Insurance, security, storage, maintaining quality and professional publications can cost the collector a significant amount of time and money. Be mindful too of risk in the provenance of the work of art. Ensuring the works are authenticated before acquiring them is strongly recommended and a must before lending.

Gifting your work(s) of art

Museums rely upon donors and collectors to further their mission in acquiring and presenting works of art. A museum's collection can be dynamic and ever-evolving, inspired and driven by the vision of its leadership. Museums also consider their place within the community in which they are based, as well as their visibility and platform for showcasing genres of art across geographies, demographics and specific times in history.

Gifting a work of art or a collection to a museum is an involved process that requires planning, negotiation and thorough documentation. It is important for the collector donor to carefully consider their own hopes, motivations and expectations before initiating the process. It is a mutual decision to make and accept a gift.

Understanding your collection and its potential place within your favorite organization is directly correlated to having established a relationship with an organization. Familiarize yourself with the organization's goals, their needs, the gift acceptance policies and the acquisition process.

What does the gifting process entail?

In determining whether gifting your collection or specific works of art is the right decision for you, know that there are several ways to part with your collection. Terms of a gift can be wide-ranging; you can gift the work of art outright now from your collection, you can make it a promised gift through a bequest, and you can determine if you should make a partial or fractional gift.

The first step in making a gift of art is to inquire with the organization if there is interest. A desire to gift your works of art does not necessarily align with the recipient organization officially accepting your gift into their permanent collection. You may discover that while your works are museum quality, they may not fit the museum's current collection goals or limitations, or the museum may only have an interest in a select few pieces of your collection.

Accepting a gift of art is a multistep process for museums. It involves review and evaluation of the artwork, negotiation and documentation of the gift agreement, and careful conservation and care of the artwork once it has been accepted into the museum's collection.

A gift (or proposed gift) of a work of art will be reviewed by an acquisitions or "collections" committee to determine whether it will enhance the museum's collection and align with the museum's mission and collections policy. The committee will consider the condition of the item and the cost of storing, displaying and caring for it. As a part of the gift, donors may also offer additional funding to establish an endowment for conservation, or for the expense of mounting an exhibition, and/or a publication of the works or collection.

It is a mutual decision to make and accept a gift.

Once the museum or organization has expressed interest in accepting the collection (or you have accepted its gift request), the collector and institution negotiate the terms of the gift. This includes: the scope of the gift, conditions or restrictions, any legal requirements, and the donor's wishes regarding the display and use of the collection. The institution will prepare a gift agreement, similar to a loan agreement, with distinct stipulations regarding the acceptance of the gift of art.

Gifting works of art

Gifting considerations

When gifting works of art, take into consideration the legal and tax efficiencies, as well as the emotions associated with gifting your art or collection.

Questions to consider when gifting works of art, in part or as a full collection:

- Do I want to gift to an organization or to my family?
- Have I discussed this consideration with family?
- Has the collection been valued and assessed?
- Where should I give my works of art? Do I have a connection to an institution? Can it accept my collection?
- Do I want my collection to be accessible to the public for view, research or education?
- Do I have a strong relationship with an organization and do I feel that it knows me well? Is my collection aligned with its mission?
- Have I created a gifting plan, and does it include both the art and the related care for the collection?
- Should I support an organization with an endowment?
- Does the gift agreement (legal documentation) outline mutual acceptance and disposition of the works of art?
- Do we gift now with a full or partial art transfer in life, or is this a gift by bequest?
- Do my advisors and executors understand my wishes and the process of gifting?
- Will the organization accept my works of art into its collection, or will they sell or both?
- How will I be recognized for my gift?
- Will the work of art be included in a publication? If so, what will the acknowledgment consist of?

In summary as it relates to gifting your work(s) of art

Ensure the lifecycle of your art collection is outlined in the gift agreement, and understand the museum's ability and limitations in accepting gifts of art. Ask questions, have open communication with both the organization and your family, and establish a plan. The emotional or sentimental significance of the collection cannot be overstated, neither can the importance of legacy, nor even the implications of recognition related to the collector and collection. While gifting a collection will inevitably include emotional and personal elements, the donor should also consider the tax benefits, the philanthropic component, community appreciation and the significance of making the collection available for public view.

A subset of collectors who embark on the journey to explore gifting part or all of their collection will learn in that process that the receiving museum will divide up or only partially accept their carefully curated collection. If this is not an attractive or viable way forward in order to ensure an intact legacy, some collectors may look to establish their own public institutions to house their private collections.

Małgorzata Mirga-Tas
Andro Drom (On the Way), 2016
Textile, acrylic paint, mixed media, on wooden stretcher
UBS Art Collection

Photo credit. Nicolas Duc

To keep in mind:
A museum’s perspective

Museums serve as repositories of cultural pieces; they help care for and preserve art works in perpetuity and ensure they continue to be available for future generations to enjoy. However, museums have limited space and only a small percentage of their total collections are available to be on public view. Similar to how one might rotate art displayed in the home based on décor, change in room function or seasonality, so too might a museum. As one curates the art showcased in a home and places some items in storage, so does a museum.

Donors often express concern when learning that their personally meaningful pieces may spend a significant amount of time in art storage. As a part of the collections committee assessing the gift, the works of art may be accepted but may not be immediately placed on view until there is a relevant platform to share the works. Timing around actual display and length of time on display may also not be committed to at the time the gift is made.

In fact, there are several options on the part of the recipient organization. The museum may accept your gift of art and place it into its collection, it may accept the work of art or collection with an understanding it will sell, it may accept some works to keep and some to sell, and lastly the museum may decline the gift altogether.

Selling works of art from its collection is known as deaccessioning, and it is a common practice for museums. A museum or organization will sell a work of art and use the proceeds to purchase new works of art, or to add to an art acquisition fund. As a part of the gift acceptance policies and a gift agreement, your gift should outline the stipulations for accepting works of art and outline a deaccession plan to allow for a curated collection. This could include the museum’s ability to sell and use the proceeds to create a fund to purchase works in the name and spirit of the collector donor.

In addition to deaccession, museums must winnow down their collections for a myriad of other reasons: a process that is often not understood by many donors or the executors of their estates. Collectors want the affirmation that their collecting eye was “museum quality,” as well as the pride of gifting their art for view in a museum.

Museum collections are dynamic and are refined and shaped to complement the permanent collection, thus informing when and how to part with certain works of art. Pieces can be removed from a permanent collection due to their provenance, authenticity or attribution of the work, or if determined to have been stolen, illegally imported or misappropriated. The need for conservation and the cost of maintaining the work of art may exceed the available funds at the institution, resulting in a sale.

Displaying in communities

Art can bring joy to the collector, as well as to the people they share it with. For many collectors, there are multiple benefits to sharing the works they own. You can display in the community or loan a partial or full collection to another entity. Just as with owning and loaning as noted earlier, some of the considerations are the same for an individual collector or for a private foundation.

There are many ways in which to display your art in a community, and having a thoughtful strategy can help. The more obvious include museums, universities and galleries that you are likely familiar with. Additionally, you might consider other sites such as schools, municipal buildings, libraries, town halls or other public spaces. This creates an opportunity to integrate art more fully into the community and expose it to a broader base.

To name, recognize or anonymize—that is the question

Donor gifts (of a substantial size) typically fall into one of three categories:

- **Naming opportunity:** A donor may want to be recognized for a significant contribution. Such opportunities can include a capital campaign (i.e., have a building, wing of a hospital or park bench named for them). This can be a complex negotiation and might require considerable expertise to navigate (see *Negotiating charitable gifts*, a UBS publication).

- **Name recognition:** A donor may want to be included on a list of supporters for a specific program, an exhibition, on site and/or listed on the website of the arts-related charity they support.

- **Remain anonymous:** A donor may prefer to remain anonymous. As an aside, true anonymity would not be possible via a direct gift or through a private foundation. An alternative charitable vehicle (such as a donor-advised fund) would need to be utilized for complete discretion (see *Charitable vehicles: rules of the road,* a UBS publication).

Of note, a donor may be drawn to more than one of the above options, depending on the gift size and purpose.

You have built a carefully curated collection … now what?

Building your collection can be a thrilling experience—in search of the next piece, carefully curating to a certain theme or even just purchasing pieces that speak to you. You have spent so much time building, enjoying and living with the collection that it is likely you have not given much thought about what comes next. If your objective is to keep the collection together, you can gift it to your beneficiaries, create your own museum or gallery, or keep it for private enjoyment. Alternatively, you can gift it to an institution or sell your collection.

The relationships you have developed with art consultants, museums and galleries are a good place to begin your assessment into options for the future of your collection. One of the first big strategic decisions you will need to consider is whether you want to keep the collection intact, or if you are open to having it divided and therefore make decisions regarding each piece. To be sure, as this stage of evaluation will likely prove to be emotional and challenging, it is encouraged to temper the sentimentality when exploring your options. If family members have expressed interest in some or all of your collection, this could add a layer of complexity to your decision, or it may simplify matters. When making these decisions, you should engage your most trusted advisors throughout the journey.

One definitive way to keep your collection together is to create a private operating foundation, or museum, to house and show your works of art. There may be tax benefits to this strategy as well, such as a potential income tax deduction equal to the fair market value of the art and removal of the assets from your taxable estate. It is important to note that you are creating an operating business. This will require a physical building, employees and all of the logistical demands associated with ensuring that the building is open to the public for the viewing of your collection.

Questions to consider (regarding the set-up of your own museum):

Where will it be located?

- You have to select a geographic location as well as a physical building.

Who will operate it?

- Do you have family members who are willing to take on the operating responsibility, will you need to hire staff or both?

Which pieces will be housed in it?

- Will you gift your full collection?

What other funding is needed to sustain the museum?

- Will you sell some pieces to cover operating expenses?
- In addition to building and staffing costs, what are the costs of covering the storage, insurance and care of your art?
- Will you charge an admission fee?

These questions can guide important conversations with those you plan to bequeath the museum to. It is important to identify beneficiaries who will want and are able to oversee and sustain your vision.

If there is no interest in running a museum, you can consider establishing a non-operating foundation that can own, loan or sell your works of art. The process for each is the same as if done by individuals. However, private non-operating foundations are subject to a number of specific tax rules as further discussed in the last chapter of this publication.

If the goal is to sell your collection during your lifetime or as part of your estate plan, this can be done through private sale, working with an auction house or engaging directly with a museum or gallery. Many auction houses will work with you or your estate to create a catalogue and organize an auction for your collection.

It is important to remember that if you have chosen to divide your collection, you will make decisions regarding each piece as a part of your planning. To that end, you might identify a select number of pieces to preserve in a foundation or pass down to family members, others which you plan as gifts to museums, and ultimately sell the rest.

Art and private foundations

Traditionally, private foundations need to gift 5% of their previous year's average assets.

This includes the value of the art owned within the foundation. If the art is being loaned out to a museum or other entity for public enjoyment, it is counted as a charitable use asset and removed from the calculation for the minimum distribution requirement.

This is a benefit for the foundation as art is typically not generating interest as traditional investments do, and therefore can create a liquidity problem with respect to the 5% distribution requirement. In addition, it is a wonderful way to further the legacy of the family.

Legacy and lifecycle

When you have spent a lifetime acquiring pieces and building a collection, there are sentiments and emotions tied to your art. It is important to emphasize that you are likely not the only one who has strong feelings tied to a particular piece or perhaps to your collection as a whole. Your children or grandchildren might feel drawn to a piece or recall a fond memory of times shared together every time they view a particular painting. When considering making gifts of your collection—in its entirety or just individual pieces—it is important to have open communication with those who might have a vested interest.

What you decide to do is ultimately still your decision, but you might uncover something about your family as it relates to the collection during the discussion phase. Your trusted advisors can be helpful in navigating these conversations.

When your collection is considered to be a "family collection," having a discussion around it writ large, as well as exploring sentimental connections to particular pieces, can be helpful. This is a critically important conversation to have, and to discuss pieces someone might want to keep in their home or pass down their family tree in order to avoid gifting away a family favorite.

Here are a few questions to evoke a meaningful discussion about your collection:

- How will your family feel if the pieces are no longer owned personally by the family?
- What if the pieces are gifted but still tied to the family legacy?
- If you gift some pieces to a museum, how do you determine which ones, and how will your family feel about that?
- If you gift to children or grandchildren, will you aim for equal financial value in the gifts, or is it about sentimental value?

How you wish to proceed with the future state of your collection is a very personal decision. When you've determined how and where to allocate, consider bringing your family together to share your intentions and rationale. If your decision is part of your estate plan, you may want to write a letter to accompany it and explicitly share your choices and reasons with family. Gifting art to family can add a layer of complexity as it relates to thinking about equal versus equitable treatment for the recipients. What happens if one of your children has a profound connection to a piece of art of significant value, another child wants to keep a piece in their home that has a lesser value, and one does not care about art at all? You might shift other assets in your estate so that what is passed on is considered equal, or you might decide that as it relates to art, you are focusing on what is equitable. In other words, everyone gets the piece that they desire or an appropriately determined alternative. In this instance it would be important to be transparent and communicate the rationale behind a decision.

Open communication helps to minimize conflict, and it also gives you the opportunity to explain the "why" behind such decisions to your family. Without explicit clarity, there is the inherent risk that certain family members will make assumptions about your allocations that may be incorrect and not match your intent.

Thus far the emphasis has been on the journey of the collector as it relates to the evolution of the collection itself. The act of collecting can be a vehicle for purpose and impact, and your passion for the arts can extend beyond your personal collection. Here we are placing an intentional focus on how one can simultaneously move the needle and have impact on the arts more broadly.

Going beyond: having an impact on the arts

Are you interested in how art can serve as a meaningful platform for driving awareness or support for a particular cause? Do you want to support artistic expression that highlights certain social or environmental issues? Do you want to cultivate partnerships with other arts organizations? Do you want to provide access to the broader population for exposure, enjoyment and/or educational purposes? Do you want to create opportunities for younger generations or under-resourced populations?

This is by no means an exhaustive list but can serve as the early stages of self-inquiry into how to build a holistic approach to supporting arts and culture. There are many ways to incorporate a philanthropic lens into your overall support of the arts. Is there a consistent throughline to your strategy? For example, collecting art from female artists and simultaneously supporting girls and women in philanthropic endeavors, or supporting artists who use recycled materials to bring attention to climate change.

You can invest beyond the collection, especially if it has a very specific and targeted emphasis. This may be attractive if your interests in supporting the arts community is more expansive or includes other mediums, demographics, geographies or time periods.

Collectors can give their time and/or funding for specific education and arts programming, in both the visual and performing arts. Community organizations will often collaborate to promote new works of art, a community-wide program, special exhibitions and musical performances programs. A good place to start (or to continue your reflection) is to consider the following questions, which we've categorized into three segments: What, How and Who.

What

- What is/are my passion(s) within the art world, as this can extend beyond visual arts?
- Do I have an interest in utilizing my art collection and platform for broader support to the arts community?
- Does this translate into the difference that I seek to make?
- What brings me joy as it relates to art (both for myself and for others)?

How

- How will I seek to have an impact or effect change?
- How can I support individuals in the form of a fellowship or scholarships?
- Do I want to create a dedicated fund or endowed program?
- How can I fund a capital project or program?

Who

- Who will join me?
- Will you involve family, friends, extended members of your community?
- Will you seek other arts funders to partner on your efforts?
- Will you consider joining other philanthropists in a giving circle?

Who/what do I want to support?

- Directly to those creating art
- By making art more widely accessible—for education and enjoyment purposes; or
- Providing access and creating opportunities for others to explore embarking on an artistic path

In all of the above pursuits, with which demographic(s) do I want to focus my philanthropic efforts?

- Create/expand arts programs for children (in/beyond school programs)
- Those already demonstrating creativity/desire to create art
- Specific populations (marginalized, indigenous, gender lens, orientation, to name a few)
- Cause-specific highlighted through the art (drawing attention, self-expression, creating access and visibility)
- Do I want to emphasize a time period, a moment in history or a certain geography and its related art?

Board service

Your personal passion may lead to an arts-related organization extending an invitation to join its board. Nonprofit organizations seek collectors for their perspectives and contributions. This can include joining committees or leading through board service. Participation increases awareness of arts initiatives, programs and public-private partnerships, and can expand collaboration with community leaders, arts organizations, corporations and other funders.

Beyond contributing funds or gifting works of art, one of the great rewards of service is developing meaningful connections and experiencing the impact of your passions throughout the arts community. When collectors bring their passions, financial support and networks to board leadership, it is mutually beneficial for the organization and collector. See the UBS publication "*Do you want to serve on a non-profit board*?" for a deeper dive into this topic.

Some questions to consider:

- Am I open to joining the board of an arts organization?
- How could my involvement benefit the organization?
- Are there board committees that would value my participation?
- How do I leverage my networks in service to the organization?
- How could I engage community leadership and support partnerships?

From a nonprofit perspective

Here are some ways in which arts organizations may benefit from a collector's wish to support the arts more broadly.

Access—Create educational programs and opportunities to experience the arts

- Partner with local schools to bring in arts programming
- Collaborate in bringing together art and art organizations

Exposure—Raise visibility for the arts in communities

- Provide for school children to experience a performance or tour a museum
- Host family art day programs, connect with artists-in-residence

Capacity building—Support for an organization to thrive

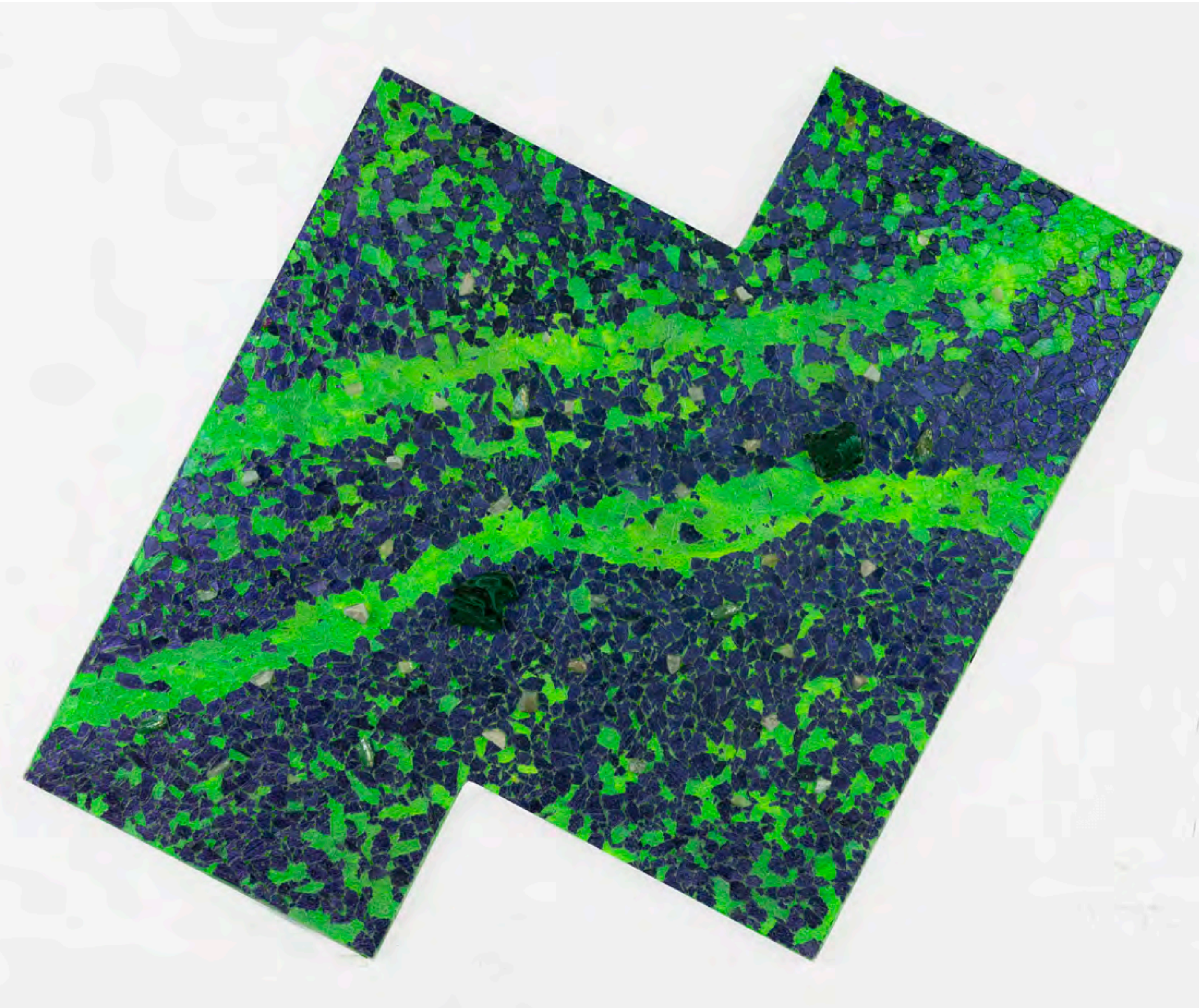
- Provide support for conservation, programming or operating needs
- Establish endowed funds for staff positions, programs and publications
- Create fellowships and scholarships to support students in the field or study of art, or creation of new art mediums
- Gift in partnership with other charities/foundations and collaborate to further any of the above

Hugo McCloud
rush hour, 2021
Single use plastic mounted on panel
UBS Art Collection

Concluding remarks

Throughout the course of a collector's journey, many expected and unexpected opportunities may arise as it relates to the purpose and future of your collection. This can include familial and legacy considerations, philanthropic endeavors and broader benefits to the public of sharing and showcasing your works of art.

There are many ways to address all of the above pathways for a robust activation of a collection, as well as a broader commitment to the arts. A collector's journey may start as an individual pursuit, and often becomes much more inclusive as the collection grows and evolves, with the spirit of wanting it to bring joy, curiosity, impact and learning for others as well.



Alteronce Gumby
Rants and Gems, 2021
Gemstones, painted glass and acrylic on panel
UBS Art Collection
Courtesy of the artist and Nicola Vassell Gallery

Estate and charitable planning for art

Advanced Planning Group

Why planning matters

Art collections can account for a significant portion of a wealthy individual's estate. Unfortunately, collectors and their advisors often fail to give adequate attention to planning for these valuable assets. This chapter highlights important steps collectors should consider in pre- and post-mortem planning for artwork, including valuing the collection, making gifts and bequests to family members, making lifetime and testamentary charitable transfers, selling the collection and liquidity planning to pay estate taxes related to the collection.[2]

Tax savings are only one factor a collector should consider when choosing planning techniques. As mentioned above, collectors typically have strong emotional ties to their collections. A collector may have spent a lifetime carefully building the collection so that it becomes part of their identity. The collector's thoughtful stewardship can keep that legacy going for generations. The collector—not their executors or family members—is best positioned to determine the future of the collection. Careful planning during the collector's lifetime is crucial to ensure their wishes are carried out.

[2] This guide focuses on the tax rules that apply to collectors. These rules often differ from the rules that apply to artists. In addition, this guide uses the term "bequest" in the colloquial sense—referring to a transfer upon death—rather than its strict legal sense.

The most difficult asset to plan for

Artwork is perhaps the most difficult asset to plan for when it comes to gift tax, estate tax and charitable planning. Aside from fairly simple outright gifts or bequests of art to family or friends, and certain charitable gifts of unique pieces of art to museums, most planning for art does not fit easily into the traditional planning strategies used for other assets, like marketable securities, real estate or closely-held business interests. For example, traditional planning for illiquid assets often involves gifts of minority interests to family or trusts, which qualify for significant valuation discounts, sometimes in the neighborhood of 35%. This allows taxpayers to transfer significant additional value when gifting these types of illiquid assets for estate and gift tax purposes. With artwork, the Internal Revenue Service (IRS) takes the position that fractional interest gifts are entitled to little or no valuation discount, as discussed below. This is one of several areas where gifts of art are either treated differently or do not fit within the normal planning parameters.

Because estate and charitable planning for art is fairly unique, it is important to have a framework for the planning alternatives available to the collector; otherwise the collector may do little or no planning. A basic framework for estate and charitable planning for art includes the following alternatives:

1. Gifts or bequests of art to family or friends during the collector's lifetime or at death;

2. Gifts or bequests of art to charity during the collector's lifetime or at death. Charitable gifts during lifetime will typically be limited to museums because of the related use requirement discussed below;

3. Selling all or part of the collection during the collector's lifetime or at death; and

4. Some combination of alternatives 1 to 3.

Finally, if art is to be gifted at death to family or friends, the collector's estate will need to have adequate liquidity to pay any state and federal estate taxes associated with the art bequests.

> Most planning for art does not fit easily into the traditional planning strategies used for other assets.

Xaviera Simmons
Sundown (Number Nineteen), 2019
Chromogenic color print
UBS Art Collection
Courtesy the artist and David Castillo Gallery

Valuing the collection

A preliminary consideration for any estate or charitable planning for art is how the items should be valued for tax purposes. For federal estate, gift and income tax purposes, the general valuation rule is that the transferred items must be valued at their fair market value. Fair market value is the price at which the property would change hands between a willing buyer and a willing seller, neither being under any compulsion to buy or to sell and both having reasonable knowledge of the relevant facts.[3] A number of factors may be relevant to valuation, including the cost or sale price of the property, sale prices of comparable items, the cost to replace the item and expert opinions. In determining fair market value, the item should be valued by reference to the market in which similar items are sold to the general public (for example, auction sales and gallery sales (to the extent such information is publicly available)).[4]

Appraisal requirements

The willing buyer-willing seller test sets forth the general rule regarding valuation of assets for estate, gift and income tax purposes. In most circumstances an appraisal of the transferred item must be provided to support the valuation. The appraisal requirements for estate tax, gift tax and income tax purposes are slightly different.

Estate tax

For estate tax purposes, if a decedent owned collectibles where any one article is worth more than $3,000, an appraisal of the items must be attached to the federal estate tax return. The appraisal must be prepared by an expert under oath and must include an itemized list of the appraised items and a statement by the executor certifying the completeness of the list and setting forth the appraiser's qualifications and disinterested character.[5]

> In determining fair market value, the item should be valued by reference to the market in which similar items are sold to the general public (for example, auction sales and gallery sales).

Gift tax

For federal gift tax purposes, an appraisal may also be a necessary element to achieve finality with respect to transfers of art and collectibles. The statute of limitations does not begin to run on a transfer of property by gift unless the transfer is disclosed on a gift tax return in a manner adequate to apprise the IRS of the item.[6] Although a full discussion of the adequate disclosure rules is beyond the scope of this publication, collectors should note that many of the requirements of the rules can be satisfied if an appraisal meeting the requirements of the applicable regulations is attached to the gift tax return reporting the transfer.[7] The appraisal must contain, among other things, a description of the property, a description of the appraisal process employed, the valuation method used and the specific basis for the valuation. Moreover, the appraisal must be performed by an individual who holds themselves out to the public as an appraiser, performs appraisals on a regular basis, is qualified to appraise the type of property being valued, and is not the donor or donee of the property (or a related person), or employed by such persons.[8]

[3] Treas. Reg. §§ 20.2031-6, 25.2512-1 and 1.170A-1(c)(2).
[4] Treas. Reg. § 20.2031-1(b).
[5] Treas. Reg. §§ 20.2031-6(a)-(b).
[6] IRC § 6501(c)(9); Treas. Reg. § 301.6501(c)-1(f).
[7] Treas. Reg. § 301.6501(c)-1(f)(3).
[8] Id.

Income tax (for lifetime charitable planning)

Even more detailed requirements may apply to the appraisal process when a charitable income tax deduction is sought. If the collector is seeking an income tax deduction for a contribution of artwork to a charity, and the value of the artwork is more than $5,000, then the collector must obtain a qualified appraisal and attach a summary of the appraisal to the income tax return taking the charitable deduction.[9] This qualified appraisal must be dated no more than 60 days prior to the date of contribution and generally received no later than the due date for the return.[10] For art valued at $20,000 or more, the return must include a copy of the signed appraisal in addition to the appraisal summary. If any single piece of art is worth $20,000 or more, the IRS may ask the donor for a photo of the donated property, preferably an 8x10 inch color photograph, or a high-resolution digital image to fully show the object.[11] For contributions of more than $500,000, the qualified appraisal itself must be attached to the return.[12]

A qualified appraisal for charitable deduction purposes must contain detailed identifying and documentary information concerning the contributed property, the circumstances of the reported contribution, and the methodology and basis for determining the fair market value of the property.[13] Moreover, the appraisal must be completed by a qualified appraiser, defined as an individual with verifiable education and experience in valuing the type of property for which the appraisal is performed.[14] As with a gift tax appraiser, a qualified appraiser for this purpose may not be related to or regularly employed by the donor or the charitable donee. Additionally, the appraiser may not be a party to the transaction by which the donor acquired the property being appraised (unless the property is donated within two months of the date of acquisition and its appraised value does not exceed the purchase price), and, generally, no part of the appraisal fee can be based on a percentage of the property's appraised value.[15] The above requirements for a qualified appraisal must be scrupulously followed; failure to follow the requirements of a qualified appraisal or the timing of receipt and filing of the appraisal will result in loss of the charitable deduction.[16]

> A qualified appraisal for charitable deduction purposes must contain detailed identifying and documentary information concerning the contributed property.

Art advisory panel

In the event of an audit of an estate, gift or income tax return reporting a gift of a painting, drawing, print, sculpture or furnishing with a value of $50,000 or more, the auditing agent must refer the valuation to the IRS Art Appraisal Service unit (AAS) for a possible referral to the Art Advisory Panel (the panel).[17] The panel will provide a recommendation on value to the AAS and, if accepted, the recommendation will become the official position of the IRS on valuation. Advisers can help achieve the best possible result from the panel by ensuring that a comprehensive appraisal prepared by an expert in the particular work being appraised is attached to the tax returns reporting the transfer, including detailed descriptions and clear photographs of the objects appraised, a careful analysis of comparable works that have sold near the valuation date and substantiation of the work's authenticity or any questions relating to authenticity.[18]

[9] IRC §170(f)(11)(C).
[10] Treas. Reg. §§ 1.170A-17(a)(4) and (a)(8).
[11] See Instructions to Form 8283.
[12] §170(f)(11)(D); Treas. Reg. §1.170A-16(e)(1)(iv).
[13] Treas. Reg. § 1.170A-17(a)(3).
[14] Treas. Reg. §§ 1.170A-17(b)(1)-(b)(4).
[15] Treas. Reg. § 1.170A-17(b)(5).
[16] Elizabeth Carrott Minnigh and David E. Stutzman, *Planning for Authors, Musicians, Artists, and Collectors* (BNA Portfolio 815-3rd), III.E.4.b.
[17] IRM 4.48.2.2(1). For purposes of this guide, "IRM" means the Internal Revenue Manual.
[18] See Manuel E. Gonzalez and Michael L. Duffy, "Valuing Art," *Trusts and Estates* (February 2005), p. 57.

Advance ruling

If a collector wants advance certainty regarding the IRS position on valuation prior to filing a return, they can utilize the procedures described in Revenue Procedure 96-15. Under that revenue procedure, a taxpayer can obtain an advance ruling from the IRS on the value of tangible personal property for income, estate or gift tax purposes. In order to obtain a ruling, the following requirements must be met:

1. First, the ruling request must be made after the property is transferred.

2. Second, the taxpayer must already have obtained a qualified appraisal.

3. Third, at least one of the items transferred must have a value of at least $50,000.

Fourth, a copy of the appraisal plus a photograph of the artwork and a description of the item must be attached to the ruling request.[19]

The fee for an advance determination is $7,500 for the first three items and $400 for each additional item as of the date of writing.[20] Once the advance ruling is given, it is generally binding on the IRS, provided there are no material misrepresentations. The collector can still dispute the ruling by submitting further information.

Penalties for incorrect valuations

For income tax purposes, the Internal Revenue Code imposes an accuracy related penalty for any substantial valuation misstatement. If the valuation as reported is 150% or more of the valuation as ultimately determined, the penalty is 20% of the underpayment of tax. If the valuation as reported is 200% or more than the valuation as ultimately determined, the penalty is 40% of the underpayment of tax.[21] The penalty may be waived if the taxpayer shows there was reasonable cause and the taxpayer acted in good faith.[22]

For estate and gift tax purposes, the Internal Revenue Code imposes a 20% penalty if the value as shown on the return is 65% or less of the value ultimately determined, and a 40% penalty if the value as shown on the return is 40% or less of the value ultimately determined.[23] The IRS can waive the penalty if the taxpayer establishes that there was reasonable cause for the valuation and they acted in good faith.[24]

[19] Rev. Proc. 96-15.
[20] Rev. Proc. 2023-1, Appendix A, Paragraph (a)(9).
[21] IRC §§ 6662(a), 6662(b)(3), 6662(e)(1)(A), 6662(h)(1), and 6662(h)(2)(A)(i). For these penalties to apply, the valuation misstatement must cause the underpayment of tax to exceed $5,000. IRC § 6662(e)(2)).
[22] IRC § 6664(c)(1). The accuracy related penalties also apply to other types of misconduct, including substantial understatements of income tax and negligence, among others, which could also be implicated by an incorrect valuation of artwork. See, e.g., IRC §§ 6662(b)(1)-(2). However, the maximum penalty is still 20% or 40% of the underpayment, whichever rate is applicable, even if the underpayment is due to multiple forms of misconduct. Treas. Reg. §1.6662-2(c).
[23] IRC §§ 6662(g)(1)-(2), 6662(h)(1), and 6662(h)(2)(C). For these penalties to apply, the valuation misstatement must cause the underpayment of tax to exceed $5,000. IRC § 6662(g)(2)).
[24] IRC § 6664(c)(1).

Non-charitable planning during lifetime

Many collectors would like to keep all or a portion of the collection in the family after their deaths. In situations where there is appreciation potential, it may make sense for the collector to give the items away during their lifetime, since all future appreciation from the time of the gift onward is removed from their taxable estate.

When contemplating making a gift, it is important to keep the income tax basis rules in mind. As a general rule, giving away assets during life eliminates the opportunity for a "step-up" in income tax basis at death. The income tax basis of an asset is used to determine the gain or loss upon sale. Under current tax law, the income tax basis of assets held at death is adjusted to the then fair market value. The basis step-up can be very favorable for heirs or beneficiaries because adjusting basis to fair market value eliminates income tax on any "built-in" gains associated with the inherited property.[25] The heir or beneficiary can then immediately sell the property and pay no capital gains tax.

The step-up rule does not apply to assets that are given away during life. Instead, lifetime gifts are subject to carry-over basis, meaning the donee takes the donor's basis in the appreciated property.[26] Thus, the donee will be taxed on all appreciation when the donee ultimately sells or disposes of the asset.

If a collector determines that a lifetime gift still makes sense despite the loss of a step-up in income tax basis, the Internal Revenue Code provides the collector with tools to help plan in a tax-efficient manner. These tools include the annual gift tax exclusion and the exemption from the gift, estate and generation-skipping transfer (GST) tax, outlined below.

Tools for gifting art to family

Current federal law encourages making gifts by providing several tools that can be used by a collector during their lifetime, as long as certain requirements are met.

[25] In the case of depreciated property, the basis adjustment rules may result in a step-down in income tax basis, eliminating the ability of an heir or beneficiary to take advantage of a capital loss. In certain situations, it may be beneficial to sell loss property prior to death to take advantage of the capital loss income tax benefit. This guide uses the term "heir" in the colloquial sense—referring to a person who receives property from a decedent—rather than its strict legal sense.

[26] In the case of gifts of depreciated property, basis will equal fair market value at the time of the gift if the property is ultimately sold below the donor's basis.

Annual exclusion gifts

Federal law allows any individual to transfer up to $17,000 annually (in 2023, indexed for inflation) to anyone without eroding that individual's lifetime exemption (*discussed in the next paragraph*). A married couple may, potentially, transfer up to $34,000 per person. For a gift to qualify for the annual exclusion, it must be a gift of a present interest. According to the Treasury Regulations, the recipient must have an "unrestricted right to the immediate use, possession, or enjoyment of property."[27] That's easily satisfied in the context of an outright gift of art to a family member but becomes more complicated in the context of gifts to an irrevocable trust.

Technically, a gift to an irrevocable trust generally doesn't qualify as an annual exclusion gift because it's considered to be a gift of a future interest. That's where a couple named Mr. and Mrs. Crummey come in. The Crummey's attorney helped popularize an estate planning concept that allows gifts to an irrevocable trust to qualify as an annual exclusion gift. The attorney accomplished this by providing in the trust document that the beneficiaries of the trust had the right to withdraw amounts that were contributed to the trust for a specified period of time after the amounts were contributed in a particular calendar year, creating a present interest gift. Fortunately, the court in the Crummey case endorsed this strategy and the IRS acquiesced, and thus was born the "Crummey power," which permits annual exclusion gifts to be made to irrevocable trusts as long as certain language is included in the trust agreement.

Lifetime exemption

Any art transferred to family members that doesn't qualify for the annual exclusion (for example, if the gift is over $17,000/$34,000 per person) will use the collector's lifetime exemption. The amount of this exemption is $12.92 million (in 2023, indexed for inflation and scheduled to sunset after December 31, 2025).[28] The gift and estate tax exemption amounts are unified. Simply put, the gift tax exemption is used during life and the estate tax exemption is used at death. That means that the collector can:

1. Give it all away during life, leaving no estate tax exemption;

2. Give away a portion during life, leaving the remaining exemption available to use at death; or

3. Give none away during life, leaving the entire exemption available at death.

Any amounts in excess of the exemption are generally taxed at a flat 40% rate at the federal level (unless such transfer qualifies for the marital deduction or the charitable deduction). Many states have their own estate taxes that are in addition to the federal estate tax (but are deductible against the federal taxable estate); one state, Connecticut, has its own gift tax.

> Any art transferred to family members that doesn't qualify for the annual exclusion (for example, if the gift is over $17,000/$34,000 per person) will use the collector's lifetime exemption.

Generation-skipping transfer tax exemption

While the lifetime exemption applies to the collector's assets that are given during lifetime or at death, the GST tax exemption is typically used to avoid tax at the collector's children's or grandchildren's deaths. To understand the GST tax exemption, it's important to provide some context. Soon after the federal estate tax was enacted in 1916, attorneys for wealthy families found that there was a gaping loophole.

The estate tax applies to everything an individual owns at death. What if a wealthy parent paid estate tax at their death and left their child's inheritance in an irrevocable lifetime trust for the child's benefit, and when the child died, the assets continued in trust for their children? The trust's assets weren't included in the child's estate because they didn't own them even though they could benefit from them. The assets were owned by an irrevocable trust that continued at their death for the benefit of their children.

[27] Treas. Reg. § 25.2503-3(b).

[28] IRC § 2010; Tax Cuts and Jobs Act of 2017. The gift and estate tax exemption is indexed annually for inflation and currently includes a temporary increase. This increase expires after 2025, at which time the gift and estate tax exemption for US persons will be cut roughly in half. Unless explicitly stated otherwise, this guide assumes a collector or other individual is a US person for US tax purposes.

In 1976, Congress enacted the first GST tax, and then adopted the current version in 1986 to close this and other end-runs around the estate tax. Basically, the GST tax provides that an irrevocable lifetime trust like the one described above will be subject to a 40% tax (same as the estate tax at the child's death). But, because Congress gives an exemption from the estate tax, it's only fair that it gives an exemption from the GST tax as well. The amount of the GST tax exemption is also currently $12.92 million (in 2023, indexed for inflation and scheduled to sunset after December 31, 2025), exactly the same amount as the lifetime exemption. It's a second exemption that can be layered on top of the lifetime exemption. For example, the collector could transfer art to an irrevocable lifetime trust for the benefit of their children in the amount of $12.92 million. The taxpayer would file a federal gift tax return (Form 709) and elect to allocate GST tax exemption to the trust in the same amount. There are also rules that will automatically allocate GST exemption to trusts if the trust agreement contains certain provisions. The result would be that the trust would be exempt from the GST tax, no matter how significantly the trust assets appreciate, for as long as state law allows the trust to continue—essentially 90 to 100 years in most states. Additionally, at the time of writing, 24 states allow perpetual trusts, and 11 states allow quasi-perpetual trusts.

Unlimited marital deduction

In addition to the annual exclusion and exemptions described above, federal gift and estate tax law also permits unlimited bequests and gifts between US citizen spouses. This concept, known as the marital deduction, allows a taxpayer to transfer an unlimited amount of assets to their spouse either during life, or at death, without using any portion of their lifetime exclusion.[29] The transfer may be made outright to the spouse or in trust for the spouse's benefit provided that the trust is structured in such a way so as to meet several requirements. The unlimited marital deduction is not available for outright gifts or bequests to a non-US citizen spouse, but is available for a transfer in trust for the benefit of a non-US citizen spouse provided the trust meets certain requirements (i.e., it qualifies as a qualified domestic trust).

> The goals for tax-efficient wealth transfer are threefold: removing value, freezing value and locking in the higher exemption values.

Tax goals of gifting art to family

The goals for tax-efficient wealth transfer are threefold: removing value, freezing value and locking in the higher exemption values.

Removing value

Removing value from the transfer tax system is difficult to do in the context of transferring art. In most cases, if an individual makes a lifetime gift, that gift (valued as of the date of the gift) is technically included in determining the amount of the estate at death for estate tax purposes. The lifetime exemption is then used to reduce the size of the taxable estate. However, there are three exceptions to this general rule.

1. First, if the collector makes a gift using their $17,000 annual gift tax exclusion, the gift is completely removed from the taxable estate.

2. Second, if the collector transfers a fractional interest in an illiquid asset, they may be entitled to valuation discounts substantiated by a qualified appraisal for lack of control and lack of marketability, among other factors. These discounts may sometimes exceed 35% depending on facts and circumstances, effectively removing that amount from the taxable estate, as long as the transfer or the valuation discount is not challenged by the IRS upon audit. Unfortunately, the IRS and the courts typically take the position that little or no valuation discounts are permitted for fractional gifts of art. See the section on *Valuation discounts for fractional interest gifts*, below, for further discussion on this point.

3. Third, if the art is transferred to an irrevocable trust that will not be included in the collector's gross estate, the trust can be drafted so that the trust creator can pay the trust's income taxes during their lifetime, as opposed to having the trust be its own separate taxpayer. This effectively reduces the collector's taxable estate by the taxes paid on behalf of the trust without being considered to have made a gift. This is known as a "grantor trust," and this technique is highly effective in removing value from the collector's taxable estate.

[29] IRC §§ 2523 (relating to transfers during the taxpayer's lifetime) and 2056 (relating to transfers at death).

Freezing value

Freezing value involves the collector making a gift (outright or in trust) using some or all of their gift tax exemption. On the collector's death, the amount of exemption used to make the gift is brought back into the estate for purposes of calculating their estate tax as described above. Any appreciation on the gift from the date of the gift until the collector's death is excluded from the taxable estate. That is to say that the collector succeeds in "freezing" the value of the gifted property for estate tax purposes at its date-of-gift value rather than at its date-of-death value.

Locking in the higher exemption

On January 1, 2018, the gift, estate and GST tax exemptions doubled under the Tax Cuts and Jobs Act of 2017. Unfortunately, because of certain Senate procedural rules, the higher exemptions will "sunset" without additional Congressional action at the end of 2025. This means that the exemptions will return to where they were prior to the new law (indexed for inflation). If, however, the collector uses a portion or all of the higher exemption amounts by making gifts prior to the sunset date, those amounts transferred in excess of the exemption amount immediately before sunset generally will be locked in and exempt from transfer tax going forward pursuant to guidance from the IRS.

Valuation discounts for fractional interest gifts

Let's assume that a collector has three children and would like to gift a valuable painting to all three of them to share. The collector gifts a one-third interest in the painting to each child, so that each will be able to hang the painting on a wall for four months a year. As discussed above, for most illiquid assets (e.g., real estate or a closely held business), a gift of a minority interest in the asset would reduce the appraised value significantly, because an unrelated third party would typically not be willing to pay full value for it. Unfortunately, in the context of fractional gifts of art, the IRS has taken the position that little or no discount is available, and courts have generally agreed.[30]

For example, in *Estate of Scull v. Commissioner*, the Tax Court held that a 5% discount from pro rata fair market value for a fractional interest in artwork was appropriate for estate tax purposes. That case involved an art collection that was the subject of divorce-related litigation, which resulted in a court order for the collection to be split 65%/35% between husband and wife. The husband then died, and his estate argued that the fractional interest in the art collection should be reduced by a discount of 15% for estate tax purposes. The court disagreed, holding that a discount of 5% was sufficient to address any uncertainties in acquiring the fractional interests.[31]

[30] See, e.g., Rev. Rul. 57-293, 1957-2 CB 153 Ex. 2 (donation of fractional interest in artwork resulted in income tax deduction equal to the fractional interest multiplied by the value of the artwork with no discount); *Stone v. US*, 2007-2 USTC ¶60,545 (N.D. Cal. 2007), *aff'd in unpub. op.*, 103 AFTR2d 2009-1379 (9th Cir. 2009); *Estate of Scull v. Commissioner*, T.C. Memo. 1994-211 (Tax Court 1994); *but see Estate of Elkins Jr. v. Commissioner*, 767 F. 3d 443 (5th Cir. 2014).

[31] *Estate of Scull v. Commissioner*, T.C. Memo. 1994-211 (Tax Court 1994).

Similarly, in *Stone v. US*, the court permitted a 5% fractional interest discount in determining the estate tax value of the decedent's undivided 50% interest in a 19-piece art collection. The estate argued that a 44% fractional interest discount should apply since a buyer would not be interested in purchasing only half of an interest in each piece of artwork. However, the court held that a hypothetical seller of an undivided fractional interest in a piece of art would likely exercise their right to partition and force the sale of the entire collection, rather than accepting a significant discount on the fractional interest. The court did acknowledge that some discount was appropriate to allow for fees and legal costs, as well as the uncertainties involved in waiting to sell the collection until after a hypothetical partition action was resolved. In its supplemental opinion, the court affirmed its original opinion that a "relatively low" 5% discount was appropriate.[32]

Following the *Stone* case, which was affirmed by the US Court of Appeals for the Ninth Circuit in 2009, estate planners generally became comfortable with a 5% discount on fractional gifts of artwork for estate tax purposes.

In 2014, the US Court of Appeals for the Fifth Circuit in *Elkins vs. Commissioner* surprised the estate planning community by holding that the estate of a prominent Texas art collector was entitled to significant valuation discounts for fractional gifts of art. The facts of the case were extremely complex, involving transfers of art to a grantor retained income trust, as well as co-tenancy agreements among the owners and lease agreements with the estate to display the art, both of which prohibited the sale of the art without unanimous consent of the co-owners. The estate presented exhaustive data on the prices and rationale for discounting each piece of art based on the opinions of reputable experts. The IRS took a no-discount position, arguing that the relevant estate tax valuation regulation required an analysis of the retail market to determine value, and there was no retail market for partial interests in artwork. However, the IRS did not present any expert testimony to support this position. The Tax Court disagreed with both the IRS and the taxpayer and applied a 10% discount against the value of the artwork. The estate appealed, and the Fifth Circuit affirmed in part and reversed in part, agreeing with the Tax Court that the IRS's no-discount position was incorrect but adopting the estate's proposed discount of over 44% rather than the Tax Court's 10%.[33]

While *Elkins* had a taxpayer-favorable result, the case involved complicated estate planning as well as a taxpayer who hired multiple appraisers and was willing to take the case to court, where the IRS has the burden of disproving credible evidence. Moreover, the IRS presented no evidence to dispute the taxpayer's appraisers, a tactical mistake that it is unlikely to repeat. As a result, collectors should be very cautious in relying on *Elkins* to support a significant discount on fractional interests in artwork.[34]

[32] *Stone v. US*, 2007-2 USTC ¶60,545 (N.D. Cal. 2007), *aff'd in unpub. op.*, 103 AFTR2d 2009-1379 (9th Cir. 2009).
[33] *Estate of Elkins Jr. v. Commissioner*, 767 F. 3d 443 (5th Cir. 2014).
[34] Darren M. Wallace and Alexis Gettier, "Using Family Entities for Planning with Artwork," *Trusts & Estates*, May 18, 2016; Kristin T. Abati and Renat V. Lumpau, "Elkins: A Double Edged Sword?," *Trusts & Estates*, February 13, 2015.

It is worth noting that the marketplace for artwork is rapidly evolving, and it's possible that the prevailing views on the valuation of fractional interests in art could change along with the market. The IRS's basis for its position that there should be no or limited discounts for fractional interests in artwork is connected to the lack of a retail market for such interests. That is, because there's no established market for undivided fractional interests in works of art, the relevant market is a retail market in which all co-owners agree to sell the entire interest in the artwork with no discount.[35] In recent years, however, a more robust financial marketplace has developed for minority stakes in artwork. Investors can invest in art funds, which are professionally managed, long-term, illiquid investments like private equity funds or hedge funds that allow investors to indirectly invest in a portfolio of diversified artwork.[36] In addition, some firms are now offering investors the opportunity to own a fractional interest in one particular piece of art.[37] The availability of these types of investments could impact how fractional interests in individual pieces of artwork are valued for tax purposes in the future.

> In recent years, a more robust financial marketplace has developed for minority stakes in artwork.

Wealth techniques for gifting art to family

General

When contemplating a lifetime gift of art to family or friends, either outright or in trust, it is critical for tax purposes that the transfer is a completed gift. In order to have a completed gift, the collector must relinquish dominion and control over the gifted art and the collector must receive nothing in return for the gift. Because of the collector's emotional ties to the gifted art, they may want to retain some use of the art after the gift. This retained use will likely result in an incomplete gift for tax purposes and the gifted artwork will be included in the collector's taxable estate at their death.[38] One possible exception to this rule would be where the collector would lease back the gifted art for fair market value (*see below*).

Outright gifts to family or friends

Outright gifts of art are fairly simple. In order to have a completed gift for tax purposes, the collector must irrevocably part with dominion and control of the art by delivering the art to the recipient family member or friend, without any retained use by the collector and without receiving any consideration in return for the gift. The recipient must have full ownership of the art, with the ability to hang it on their walls, place it in storage or sell it. The art can no longer hang on the collector's walls and should be taken off of their insurance, a deed of gift should be prepared, and, if the value exceeds the annual exclusion, a gift tax return should be filed.

Irrevocable trust

Owners of more substantial collections might consider making gifts of collectibles to an irrevocable trust (e.g., a trust that the grantor cannot revoke once created) for the benefit of family members (e.g., children and grandchildren) that includes withdrawal powers (i.e., rights that permit a gift to an irrevocable trust to qualify for the annual gift tax exclusion) for each trust beneficiary. For example, a married individual with three children and six grandchildren could make gifts up to $306,000 ($34,000 for each of nine descendants) to the trust in 2023 without generating federal gift tax or eroding their lifetime estate and gift tax exemption. Any value in excess of annual exclusion gifts could be covered by the $12.92 million lifetime exemption, and, if grandchildren or more remote descendants are beneficiaries, the collector should also allocate their GST exemption.

This approach offers at least two benefits over outright gifts to the children and grandchildren. First, the donor would not have to break up the collection among individual beneficiaries in order to make the gifts. Instead, the collection could be kept intact in the hands of the trustee, with the trustee having discretion over the management and disposition of the individual pieces over time. Second, the trust could be structured as a generation-skipping trust designed to remove the gifted property not only from the donor's estate, but also from the estates of the children and even grandchildren and more remote descendants. Furthermore, since the

[35] Id; Rev. Rul. 57-293, 1957-2 CB 153 Ex. 2.
[36] Matthew Erskine, "Art and Art Funds as Alternative Investments," *Trusts & Estates*, November 16, 2022.
[37] Abby Schultz, "Buying a Piece Of Art-Market Hype." *Barrons*, June 22, 2023, *barrons.com/articles/buying-a-piece-of-art-market-hype-7c1ba913*.
[38] IRC § 2036(a)(1).

appreciation of the art then occurs outside of the taxpayer's estate (as discussed in the *Freezing Value* section above), the art or collectibles chosen to be gifted to an irrevocable trust should be works that are expected to appreciate in value. Finally, if the trust is structured as a grantor trust, the collector can continue to pay income taxes on behalf of the trust and can swap assets with the trust without income tax consequences.

Art LLC

Another approach that also takes advantage of the possible discounting available with partial gifts of artwork would be for the client to place the artwork in a family limited partnership or family limited liability company (Art LLC or LLC). The Art LLC would serve the following purposes. First, it would provide a convenient vehicle through which to manage and control the collection, regardless of who the owners of interests might be from time to time. The manager of the LLC could provide necessary services, such as maintaining adequate insurance and storing and transporting artwork safely, and may be able to assist in deriving liquidity through lease arrangements or loans. In addition, the Art LLC would create an asset with which to make equal lifetime gifts of artwork (which can otherwise be difficult with a collection of artwork with items of significantly varying values), and the manager of the LLC may permit possession and enjoyment of the artwork held in the Art LLC commensurate with each member's interest.[39]

Further, if interests in the Art LLC are gifted to family members or trusts, it may be possible for an appraiser to apply discounts to the value of the gifted property to reflect the fact that the gifted LLC interest is not readily marketable and does not permit the recipient to control the affairs of the entity. Of course, the IRS may challenge discounts taken with respect to gifts of interests in an Art LLC, just as it has challenged discounts with respect to direct gifts of artwork.[40] Moreover, collectors should be aware that the IRS and many courts have taken a dim view of family limited partnership and limited liability company planning in general. Recent cases indicate that if the client retains too much control over the LLC or the LLC lacks a legitimate business purpose, the entire value of the LLC's assets can be brought back into the client's taxable estate under Section 2036 of the Internal Revenue Code, even if some or most of the LLC interests have been given away prior to the client's death.[41] For example, in *Powell v. Commissioner*, decided in 2017, the Tax Court disregarded a transfer of a 99% limited partner interest in a family limited partnership to a charitable lead annuity trust. The court agreed with the IRS that the limited partnership interest was properly includable in the decedent's gross estate under section 2036, in part because the decedent could agree, with the two general partners (her sons), to dissolve the partnership at any time.[42] Although the facts in *Powell* are a problematic example of "death bed tax planning," the case arguably has broader relevance to planning with entities that lack a non-tax business purpose.[43]

Sale to grantor trust

A more advanced strategy involves a sale to a grantor trust. If the collection is very valuable, transfers using the annual gift tax exclusion and the lifetime exemption will not be sufficient to remove value from the client's taxable estate, even with the possibility of a discounted value using the above strategies. In those cases, a collector might consider (after funding an irrevocable trust with annual exclusion gifts or their lifetime gift and GST exemptions) a sale of additional works (or additional interests in an Art LLC) to an irrevocable trust in return for the trust's promissory note, bearing interest at least at the rate prescribed in order to avoid imputation of interest under the Internal Revenue Code. In the typical sale transaction, the note is structured so that payments of interest only are required, with a balloon payment of principal mandated in the last year of the note. If the assets sold to the trust appreciate at a rate greater than the interest rate on the promissory note, value will have been transferred to the trust free of federal gift tax.

[39] Id. There are downsides to this centralized control as well. When a collector contributes artwork to an Art LLC with multiple members, they have exchanged their direct ownership in the art for a membership interest in an entity of which the collector isn't the only member. While the collector has not entirely parted with their artwork, they won't be able to continue their enjoyment of the artwork in the same manner. Darren M. Wallace and Alexis Gettier, "Using Family Entities for Planning with Artwork," *Trusts & Estates*, May 18, 2016.

[40] Id. ("The IRS seems to be holding fast to the tenet that there's no actual market for fractional interests in art and appears unwilling to condone a discount for the value of a fractional interest in the entity vis-à-vis the value of the underlying works."); Paul Sullivan, "A Potential Game Changer for Estate Taxes on Art," *The New York Times*, October 3, 2014.

[41] See, e.g., *Estate of Powell v. Commissioner*, 148 T.C. 18 (2017). See also *Strangi v. Commissioner*, T.C.M. 2003-145, aff'd 417 F.3d 468 (5th Cir. 2005); *Turner v. Commissioner*, 382 F.3d 367 (3rd Cir. 2004). But see *Kimbell v. Commissioner*, 371 F. 3d 257 (5th Cir. 2004); Rev. Rul. 93-12, 1993-1 C.B. 202, 1993-7 IRB 13.

[42] *Estate of Powell v. Commissioner*, 148 T.C. 18 (2017).

[43] Id.; N. Todd Angkatavanich, James Dougherty, Eric Fischer, "Estate of Powell: Stranger than Strangi and Partially Fiction," *Trusts & Estates*, May 25, 2017.

It is usually advisable to structure the irrevocable trust as a grantor trust for income tax purposes for three reasons.

1. First, if the trust is a grantor trust, then the sale will not cause the grantor to recognize capital gain income.[44]

2. Second, as discussed above, if the art held in the trust is sold by the trustee to a third party, any gain on the sale will be taxed to the grantor on their personal income tax return, which as discussed above enhances the value of the trust but is not treated as a taxable gift.

3. Third, because the trust is a grantor trust, the interest payments on the promissory note will not be treated as taxable income to the grantor.[45]

If the trust has insufficient liquid assets when the principal on the note is due, a portion of the art originally sold to the trust could be returned to the grantor in satisfaction of the note. The art likely would need to be appraised at that time to ensure that the appropriate value was being returned to the grantor. The transaction needs to be structured carefully to ensure that it is respected properly for income, gift and estate tax purposes.

Grantor retained income trusts for non-family members

For transfers of artwork from a collector to a non-family member, a grantor retained interest trust (GRIT) can be useful. Under this technique, the collector would transfer art to an irrevocable trust, retaining the right to use the art (or the income from any proceeds of sale of the art) for a certain period of years after the art is transferred to the trust. When the term of years expires, ownership of the art passes to the collector's intended beneficiary. The gift to the beneficiary is discounted to reflect the time value of money, since the beneficiary must wait for the trust term to expire before receiving ownership of the trust property.

In a typical GRIT, the collector retains both the right to use the art and income from the transferred property for the trust term as well as a reversion to their estate in the event the collector dies during the trust term. These interests are valued using factors and interest rates promulgated under Section 7520 of the Internal Revenue Code. For transfers made in September 2023 (the time of writing), the applicable interest rate under section 7520 is 5.0%, which can result in a meaningful discount on the beneficiary's retained interests in the GRIT if the term is long enough. If the collector survives the GRIT term, the transferred art, and any appreciation on the collection, will have been removed from their taxable estate at a gift tax value of significantly less than the full value of the collection (again, assuming a sufficiently long term). The taxable gift would be lower if the GRIT term were extended, but higher if it were compressed. In addition, because the possibility of reversion is included in the valuation of the collector's interest, the value of the taxable gift would be lower if the collector were older and higher if they were younger.

[44] Rev. Rul. 85-13, 1985-1 C.B. 184.
[45] Id.

Tangible personal property GRIT for family members
The traditional GRIT technique is not effective for transfers where a "member of the family" of the collector is a remainder beneficiary because of the operation of Section 2702 of the Internal Revenue Code. "Member of the family" is defined as the collector's spouse or any ancestor or lineal descendant of the collector, the collector's spouse, the collector's sibling or any spouse of the foregoing. Under section 2702, if the collector makes a transfer to a GRIT for any member of the family of the collector, the collector's retained interest will be valued at zero, and the collector will be deemed to have made a gift of the entire interest in funding the GRIT.

An alternative trust, known as a "tangible personal property GRIT" (TPP-GRIT), may be considered for family members. Like with a standard GRIT, with a TPP-GRIT, the collector transfers art to the trust, retaining the right to use the property for a set term of years. At the end of the term, ownership of the trust property passes to the collector's family. The TPP-GRIT differs significantly, however, from the standard GRIT because of the manner in which the gift to the remainder beneficiary is valued. Under the standard GRIT, as noted above, the gift to the remainder beneficiary is valued by taking the initial value of the art gifted to the trust and subtracting the actuarial value of the collector's retained use, using the section 7520 rate published by the IRS. Thus, with a standard GRIT, the value of the taxable gift to the penny can be determined using a straightforward mathematical calculation. With a TPP-GRIT, on the other hand, the value of the taxable gift equals the initial value of the property transferred to the trust minus the fair market value of the donor's retained term interest.[46]

The term interest may be hard to value, however, since the regulations under section 2702 provide that the best evidence of the value of the term interest is actual rentals that are comparable in nature and character with the property contributed to the trust and the duration of the term interest. The fair rental value of a work of art may be extremely difficult to determine, as historically there has not been a wide market for such rentals. Little weight is accorded to appraisals in the absence of such evidence.[47] There is also a risk that upon audit the IRS will assert a lower rental value than that asserted in the collector's appraisal, resulting in a higher taxable gift and interest. Because of their uncertainties, TPP-GRITs are not very common. With the recent rise in art rentals, this may be about to change (*see below*).

> The fair rental value of a work of art may be extremely difficult to determine, as historically there has not been a wide market for such rentals.

Art rental or leaseback
As mentioned above, historically there has not been a robust commercial market in art rentals like there is for real estate. As a result, if a collector would like to lease back property gifted outright or in trust to family or friends or to establish a TPP-GRIT, any rental value would need to be based on an appraisal that might not be respected by the IRS, since, as mentioned above, the IRS will look for the appraisal to include comparable rentals in the commercial market, which may be hard to find. Because of this, the collector entering into the rental agreement or using a TPP-GRIT will have no certainty as to whether the rental agreement will trigger a gift or estate tax. This may be changing. Over the past decade, there has been a significant increase in art rentals in the commercial sector. If the market continues to develop, the IRS may at some point become comfortable with art rental agreements in the context of gifted property. Unfortunately, for now, there is no safe harbor.

[46] Ann Bjerke, *Negotiating Charitable Gifts* (a publication of the UBS Advanced Planning group).
[47] Treas. Reg. § 25.2702-2(c)(3).

Non-charitable considerations at death

Sometimes lifetime gifting isn't practicable or palatable. The income tax benefit of a step-up in income tax basis at death may be more valuable to beneficiaries where there is minimal potential for appreciation or a collector has a short life expectancy. In other instances, a collector simply can't bear to part with the collection during their lifetime. Distributions of art at death can either be outright or in trust. The following are some of the issues connected with non-charitable planning at a collector's death.

Importance of inventory and good records

It is critical that a collector keeps a good inventory of the collection along with any relevant books and records relating to the collection. This will make the life of those who administer the estate significantly easier.

Be specific

Leaving specific instructions about which family members should receive specific pieces of art or collectibles will go a long way to keeping peace in the family.

Liquidity planning

Artwork and other collectibles are illiquid assets, and it is crucial to have adequate liquidity in the estate to pay estate taxes when they are due—nine months after death. This avoids the need for a fire sale of the collection. If the collector does not have adequate liquid assets, it can be helpful to purchase life insurance outside of the estate (i.e., in an irrevocable life insurance trust) to provide liquidity to pay estate taxes. The collector could also consider leasing or taking a secured loan against the artwork to cover estate taxes. As noted above, this is another area where an Art LLC may be beneficial; by centralizing the ownership of an entire collection in one entity, it may be easier to lease the artwork or borrow against it.[48]

Avoid the moving van

While there are many legitimate planning strategies to remove the value of art or collectibles from the estate, one technique that clearly should be avoided is sometimes referred to as "moving van" planning. Here's how it works. Shortly before or after a collector's death, their children remove the valuable art and collectibles from their home or possession without reporting the assets on a gift tax return or on the estate tax return. Large estates are almost guaranteed to be audited and the estate tax examiner will expect to see a level of personal property reported on the estate tax return commensurate with the decedent's level of wealth. Auditors also routinely request copies of any insurance policies on art and other collectibles owned by the decedent. Depending on the facts of a particular situation, this type of "planning" constitutes a taxable gift or tax fraud and should be avoided.

[48] Darren M. Wallace and Alexis Gettier, "Using Family Entities for Planning with Artwork," *Trusts & Estates*, May 18, 2016.

Charitable gifts of art

Some of the most exciting planning opportunities for art and collectibles are charitable in nature. If structured properly, charitable gifts and bequests of art can be tax-efficient ways of keeping a collection intact. Unfortunately, along with the planning opportunities, there are a number of tax traps that apply to charitable transfers of artwork. The general rules are detailed below.[49]

Charitable deductibility rules—in general

Tax incentives for charitable giving

Since the introduction of the federal income, gift and estate tax charitable deductions over a hundred years ago, the Internal Revenue Code has provided significant incentives for charitable gifts and bequests. It is important to note that certain types of charitable transfers are given more favorable tax treatment than others. As we shall see, lifetime charitable gifts are more favorable than gifts at death, charitable gifts to public charities are preferable to gifts to private foundations, and gifts of appreciated property held long term are typically more advantageous from an income tax perspective than gifts of cash.

Lifetime gifts versus gifts at death

If a taxpayer were to make a charitable bequest under their will of $1 million, that amount would qualify for the estate tax charitable deduction and would not be subject to estate tax. Not a bad result. If, on the other hand, the taxpayer gave the $1 million in cash to charity during their lifetime, it would not be included in their taxable estate, and they may also benefit from a $1 million income tax charitable deduction, in effect reducing current taxable income and income taxes. That would be a better result.

Public charity versus private foundation

Charitable gifts to public charities (for example, churches, hospitals and schools) are treated more favorably by the Internal Revenue Code than gifts to private foundations (typically established by a single family or corporation). Lifetime gifts to public charities (other than gifts of tangible personal property that are not related to the recipient's exempt purposes) typically entitle the donor to a full fair market value deduction, while gifts to a private foundation (other than cash or publicly traded securities) are typically limited to the donor's basis. In addition, gifts of cash to a public charity are generally deductible at up to 60% of an individual's adjusted gross income (AGI) in the year of the gift (or 50% if the individual also makes non-cash gifts), while cash gifts to a private foundation are only deductible at up to 30% of AGI. Gifts of appreciated property held long term to a public charity are deductible at up to 30% of AGI in the year of the gift but only at 20% of AGI for a private foundation. Unused charitable deductions are afforded a five-year carry forward.

49 A full description of charitable vehicles and the charitable deductibility rules is beyond the scope of this publication. For more information, see *Charitable Giving: The Rules of the Road* (a publication of the UBS Advanced Planning Group, UBS Family Advisory and Philanthropy Services, and UBS Family Office Solutions).

Cash versus appreciated property

Many individuals use cash to make charitable gifts each year. While gifts of cash are quick and easy, they are often sub-optimal from a tax perspective. Appreciated property held long term is, typically, the most attractive form of property to give to charity during a donor's lifetime. Why is that the case? Let's look at a simplified example. If a taxpayer were to make a million-dollar gift of cash to charity, they would get a million-dollar income tax deduction. If, on the other hand, a taxpayer gave a million dollars of low-basis publicly traded stock that they had owned for more than a year, they would get a million-dollar deduction, but would also avoid tax on the built-in capital gain. This effectively lowers the cost of the gift to the donor.

Tangible personal property

When a donor contributes appreciated personal property to a public charity (such as art and collectibles), there is only a fair market value deduction if the contribution is related to the recipient charity's exempt purpose. Otherwise, a contribution of tangible personal property is deductible at the lesser of the fair market value or the donor's basis. For example, if a painting is contributed to a museum and that museum intends to add the painting to its collection (versus accepting the donated painting with the intent to sell it), it is generally deductible at fair market value because the exempt purpose of a museum is to exhibit art. If, on the other hand, the painting is contributed to the American Red Cross, the donor's deduction is limited to the donor's basis since exhibiting art is not one of the American Red Cross's exempt purposes. The related use rule only applies to lifetime charitable gifts and does not apply at death (adding greater flexibility for recipient charities including private foundations).

> When a donor contributes appreciated art or collectibles to a public charity, there is only a fair market value deduction if the contribution is related to the charity's exempt purpose.

Charitable substantiation rules

The IRS requires that donors substantiate their charitable gifts. If the donor does not have proper substantiation, the charitable deduction is denied. The substantiation rules differ depending on the amount of the charitable gift and on the nature of the property contributed. For charitable gifts of less than $250, the donor needs either a receipt from the charity, a bank record, or, for gifts of property other than cash, other reliable records. For gifts of $250 or more, the donor must have a written receipt from the charity that is contemporaneous with the gift. The receipt must also include information about whether any goods or services were received in connection with the gift, along with an estimate of the amounts that are not deductible. The charity can ignore the value of token gifts to the donor in connection with a donor's gift.

A gift of non-cash property between $250 and $5,000 requires a receipt from the charity and requires the donor to file a Form 8283 listing information about the property, such as acquisition dates, price and condition. A gift of non-cash property of more than $5,000 requires the donor to obtain a qualified independent appraisal, as discussed above in *Valuing the Collection.*

Charitable planning during lifetime

Some examples of charitable planning for art are the following:

Fractional interest gifts to charity

Historically, many of the most valuable contributions to museums were fractional interest gifts. Basically, a collector could give a fractional interest in a painting or a collection to a museum (say 10%), take a deduction and still have the right to hang the painting on the collector's walls 90% of the time. Museums rarely requested the art to be transferred to them to satisfy the museum's 10% ownership. This meant that the museum typically didn't see the art until the collector's death and the art hung on the collector's walls until death, at which time it was transferred to the museum. Unfortunately, gifts of fractional interests in a work of art are much less attractive following the enactment of the Pension Protection Act of 2006. The relevant provisions of the act provide that the value of any fractional interest gifts of art for deductibility purposes will be the lesser of fair market value on the date of the gift or the fair market value on the date of the initial fractional interest gift, prohibiting the donor from taking a deduction for appreciation in value since the initial contribution. In addition, the provision requires charities receiving a fractional interest in an item of tangible personal property to take complete possession within 10 years of the initial gift or the death of the donor, whichever is earlier, and provides penalties for failure to do so.

Bargain sales

This transaction typically occurs under circumstances where a donor would like to make a gift to a museum but can't afford to part with the piece without some financial return. The donor sells appreciated property to the charity for a price lower than its present fair market value. The donor is allowed an income tax charitable deduction for the difference between the sale price and the property's fair market value. The donor must allocate the property's income tax basis between the gift element and the sale element, based on the fair market value of each part. The donor will recognize a taxable gain on the difference between the sale price and the income tax basis allocated to the sale element, but not on the gain allocated to the gift element.

Loans

Loaning artwork to charity is a popular technique. Under a special provision of the Internal Revenue Code, a loan of artwork to charity will not generate an income tax charitable deduction and will not be treated as a taxable gift. This removes the need for the donor to obtain an appraisal of the loaned artwork. Individuals looking to loan artwork to museums and other institutions should be sure to have their advisors review the loan agreements regarding such items as the length of the loan term, insurance and other issues.

Charitable remainder trusts

Tangible personal property—such as paintings, sculpture and jewelry—can sometimes be appropriate assets to fund a charitable remainder trust (CRT). A CRT is an irrevocable trust that provides distributions to individuals during their lives (or for a term of not more than 20 years), with the remainder passing to charity. Because a CRT is a tax-exempt entity, it is an ideal vehicle to accomplish the tax-efficient diversification of highly appreciated assets. When a contributed asset is sold, no capital gains tax is generated at the time of the sale, which means that all of the sale proceeds are available for reinvestment by the trust. When an individual funds a CRT, they are generally entitled to an income tax charitable deduction equal to the present value of the charity's remainder interest. However, two tax traps associated with making gifts of collectibles to CRTs are of particular importance. First, the donor's income tax deduction is delayed until the property is actually sold by trustee. Second, the donor's income tax charitable deduction for the remainder interest will be based on the lesser of the property's fair market value and its income tax basis.

> The principal activities of most private foundations are making grants to public charities and awarding scholarships to individuals.

Charitable lead trusts

A charitable lead trust (CLT) is sometimes referred to as a charitable remainder trust "in reverse." Typically, a donor will transfer assets to an irrevocable trust, either during their life or at death, which provides that a charity shall receive a qualified annuity or unitrust interest for a set term. The term may either be expressed as a number of years or the life (or lives) of one or more individuals. The donor is entitled to a gift or estate tax charitable deduction based on the actuarial value of the charity's interest in the trust. If the CLT is established as a grantor trust for income tax purposes, the donor is also entitled to an income tax charitable deduction for the value of charity's interest in the trust. The most commonly used CLT for art and collectibles is the testamentary CLT. The testamentary CLT can be structured to provide the donor's estate with an immediate estate tax charitable deduction for the full value of the collection transferred to the trust. If the trustee sells the collection shortly after it is transferred to the CLT and reinvests the proceeds in a manner that produces investment returns greater than the discount rate mandated by the IRS to value the charitable interest in the trust, the donor's family will receive any excess appreciation estate tax free.

Private grantmaking foundations

A private foundation is a form of charitable organization that usually receives its funding from an individual or a family. Although private foundations can operate programs, the principal activities of most private foundations are making grants to public charities and awarding scholarships to individuals. The major attraction of private foundations is that the donor and the donor's family can maintain control of the entity. Along with the benefits of donor control come certain burdens unique to private foundations. A private foundation is required to make grants of roughly 5% of its assets each year and is subject to an annual tax on investment income and excise taxes if it engages in a long list of activities prohibited by Chapter 42 of the Internal Revenue Code.

Create your own museum

Lifetime gifts of art through a private grantmaking foundation are not tax-efficient because the donor's tax deduction is limited to their income tax basis. As a result, a donor may want to consider establishing their own museum for the collection. This can be accomplished through the creation of an entity known as a private operating foundation (POF). The charitable deduction for gifts of artwork made to a typical private foundation is limited to the donor's income tax basis in the property. The deduction for the same gift made to a POF may be based on the fair market value of the property, up to 30% of the donor's AGI, assuming the POF satisfies the related use requirement for the donated property. Moreover, the donor can retain some degree of control over the gifted property as a member of the POF's board of directors. Note that POF is very different from a typical private foundation, which generally exists only to write checks to other charities. To be classified as a POF, a private foundation must directly operate an active charitable program (e.g., a museum) and expend or dedicate a sufficient amount of its resources to that program. The foundation must qualify as a POF by submitting a detailed application to the IRS showing that it engages in active charitable programs, meeting the requirements of various tests set forth under the Internal Revenue Code.

Testamentary charitable gifts of art

Most of the above-described charitable gift techniques can be structured as testamentary gifts. Since no income tax charitable deduction is available to a donor for charitable transfers made at death, it is generally preferable to make charitable gifts during the donor's lifetime.

The estate tax charitable deduction was added to the Internal Revenue Code in 1918, two years after the estate tax was enacted. The estate tax charitable deduction rules are set forth in Section 2055 of the Internal Revenue Code. The estate tax charitable deduction is an unlimited deduction and is not subject to any dollar or percentage limits. A deduction is allowed under section 2055(a) from the gross estate of a US citizen or resident for the full value of bequests or transfers to qualifying recipient organizations specifically described in section 2055(a). The types of organizations entitled to receive estate tax deductible contributions are broader than the organizations entitled to receive income tax deductible contributions under section 170(c) of the Internal Revenue Code. For example, transfers to foreign charities are generally deductible for estate tax purposes but are not deductible for income tax purposes. Moreover, there is no related use requirement necessary to qualify for the estate tax charitable deduction for charitable bequests of art or collectibles.[50]

An estate tax charitable deduction is disallowed if the charitable bequest is not ascertainable at the donor's death. The seminal case on ascertainability is *Estate of Marine*,[51] where under the decedent's will, the executors had discretion to make bequests to non-charitable beneficiaries, with the residue of the estate payable to two public charities. The court denied an estate tax charitable deduction because the executors' discretion to make non-charitable bequests resulted in the estate tax charitable deduction not being ascertainable as of the donor's death. Proper drafting could have cured this problem.

[50] The one instance where the related use requirement does apply at death is if an artist (or their estate) is to obtain a gift or estate tax charitable deduction for a gift of a work of art without its copyright, the qualified organization's use of the property must be related to the organization's charitable purpose or function. IRC § 2055(e)(4)(C). Thus no deduction is allowable if an artist's estate keeps the copyright and gives the artwork to a private foundation or to a public charity for an unrelated use. This is an example of how the tax rules that apply to collectors can differ from those that apply to artists.

[51] *Estate of Marine v. Commissioner*, 990 F.2d 136 (1993), *aff'g* 97 T.C. 368 (1991).

Selling the collection

Sometimes it makes sense to sell a portion or all of the collection during the collector's lifetime or at their death. The art world is a rather byzantine and insular place; there is perhaps no one better suited to navigate the sales process than the collector themself in consultation with their advisors and attorneys. They typically know the value of the collection better than anyone and have the connections in place to execute on a sale. If not, a suitable market value appraisal of the collection is useful in determining best strategies for sales avenues. If the sale is at auction, they can negotiate the terms in advance and participate in preparing the marketing materials. Even if the collection is not sold until the collector's death, many large auction houses will negotiate the terms of the auction with the collector while they are alive; in fact in many cases specialists from the auction house will actively pursue relationships with collectors over time in anticipation of a possible future sale.

Art executor/advisor

When art in an estate is valuable, many times the executor named to administer the estate is not well versed in the art market. It may make sense to name an art executor or advisor who is an expert in the art market to help with the proper liquidation of the collection if it is to be sold.

Income tax considerations

If an art collector sells a piece of artwork that they have been holding as an investment, the sale of the artwork would result in a capital gain or loss equal to the proceeds received from the sale (net of costs of sale) less the collector's basis in the asset. The capital gain or loss may be short term or long term depending on whether the one-year holding period is met.[52] Short-term capital gains from the sale of artwork are taxed at the same federal ordinary income rates as apply to short-term gains from the sale of other capital assets, with a maximum rate of 37%.[53] However, long-term capital gains from the sale of artwork are taxed at a special 28% rate that applies to the sale of collectible items, such as works of art, antiques, rugs, musical instruments, gems and coins.[54] This 28% rate is higher than the 20% maximum rate that generally applies to long-term gains from the sale of other capital assets. The 3.8% net investment income tax would also apply in addition to any short-term or long-term capital gain on the sale of art by high income taxpayers.[55] For individuals, capital losses may only offset ordinary income up to $3,000 per year but can offset capital gains and be carried forward indefinitely.[56] State income tax would apply in addition to federal income tax on gains from the sale of artwork and would vary by state.

[52] IRC §§ 1222(1) and (3).
[53] IRC § 1(j)(2).
[54] IRC §§ 1(h)(1)(D), (h)(3), (h)(4), (h)(5), 408(m), and 1222(11).
[55] IRC § 1411(a)(1).
[56] IRC § 1211. The rules regarding the ordering of offsetting different types of capital gains and losses are complex and beyond the scope of this guide. IRS § 1(h).

If an individual purchases a piece of artwork but holds it for personal use rather than as an investment, gains from the sale of such asset would have to be recognized, but losses in excess of gains would be disallowed under the hobby loss rules.[57]

The taxpayer's basis in artwork depends on how it was acquired. If the taxpayer purchased the artwork themselves, their basis would be the amount paid for the artwork (including cash, debt obligations, and other property or services as well as sales or use tax and other expenses connected with the purchase).[58] If the taxpayer received the artwork as a gift, then the taxpayer's basis in the asset would be the same as the donor's basis in the artwork at the time of the gift.[59] However, if the gifted property is worth less than the donor's basis at the time of the gift, the donee's basis will equal fair market value at the time of gift if the property is ultimately sold by the donee at a loss.[60] If the taxpayer inherited the artwork, then the taxpayer's basis in the asset would be the value of the artwork at the time of the donor's death.[61] The taxpayer's basis, as initially determined based on the above, would be increased by additional amounts the taxpayer spent to restore or improve the artwork.[62]

There is no longer an ability to defer gain on the sale of artwork in an exchange under Section 1031 of the Internal Revenue Code. Prior to 2018, collectors were able to defer gain on exchanges of tangible personal property for like-kind personal property, but the Tax Cuts and Jobs Act limited section 1031 to real property.[63]

When evaluating the advantages and disadvantages of selling an art collection during their lifetime, collectors should carefully consider the federal and state income tax burden of a lifetime sale against the federal and state estate tax burden of retaining the collection until death. With respect to states that have very high income tax rates and no estate tax, like California, there may be income/estate tax arbitrage opportunities. Collectors who are domiciled in such states and hold highly appreciated artwork may find that there is a lower combined income/estate tax burden if they retain the collection until death, as opposed to selling the collection during their lifetime, especially if the sale would take place closely before death. Selling the collection during their lifetime would require the collector to recognize federal and state income taxes on the inherent gain in the assets, and estate tax would still be owed on the after-tax proceeds from the sale (if retained). In contrast, retaining the collection until death would subject the full value of the collection to the federal estate tax, but the heirs would take the assets at a fair market value basis, avoiding federal and state income tax on the appreciation that occurred during the collector's holding period.

> When evaluating whether to sell an art collection, collectors should carefully consider the income tax burden of a lifetime sale against the estate tax burden of retaining the collection until death.

[57] IRC §§ 183(a)-(c). Moreover, deductions from a hobby activity come within the category of miscellaneous itemized deductions, which are suspended for taxable years 2018 through 2025. IRC § 67(g).
[58] IRC § 1012(a); Treas. Reg. § 1.1012-1(a); Elizabeth Carrott Minnigh and David E. Stutzman, *Planning for Authors, Musicians, Artists, and Collectors* (BNA Portfolio 815-3rd), VIII.B.5.d.
[59] IRC § 1015(a).
[60] Id.
[61] IRC § 1014(a)(1).
[62] Since art is not generally considered depreciable property, basis in the artwork would not be reduced by depreciation deductions. Rev. Rul. 68-232, 1968-1 C.B. 79.
[63] IRC § 1031.

Other considerations

Sales and use tax

Collectors should also take into account sales and use taxes when considering the purchase, sale or other transfer of artwork. While an in-depth analysis of the sales tax rules as they relate to the transfer of artwork is beyond the scope of this publication, the below briefly provides a general overview of US state and local sales and use tax rules, with a focus on New York and California, which have two of the larger art markets in the United States.

Sales tax

Most states impose a sales tax on the in-state sale of tangible personal property, which usually includes works of art such as paintings, drawings and sculptures. Sales tax generally must be collected by the seller of the property based on the consideration paid for the property (i.e., sales price).[64]

Until 2018, sellers in most states did not collect or withhold sales tax on sales for items purchased for shipment to states in which they did not have a physical space or employees. The basis of this exception was that a seller was required to have a physical presence or sufficient contacts within a state in order for that state to impose its sales and use taxes. In 2018, the US Supreme Court overturned its own long-standing physical presence nexus rule in *South Dakota v. Wayfair, Inc.*, upholding South Dakota's sales tax statute, which taxed remote sellers who either made more than $100,000 in gross sales from items delivered in the state or delivered more than 200 or more items to the state within a 12-month period.[65] Most states have since passed similar "economic nexus" legislation requiring remote sellers with an economic presence in their states (based on some variation of the gross sales or items delivered standard) to collect and remit sales and use tax.[66]

The *Wayfair* decision has had a significant impact on the art community, since art dealers regularly arrange shipments of artwork to states where they lack physical presence but have an economic presence (i.e., ship more than $100,000 worth of product into the state). Those dealers are now required to collect and withhold sales tax on behalf of states where they may only engage in a handful of transactions.[67] In a survey of art dealers by the Art Dealers Association of America in 2021, the *Wayfair* decision was listed as one of dealers' top concerns.[68]

Most states impose a sales tax on the in-state sale of tangible personal property, which usually includes works of art such as paintings, drawings and sculptures.

Exemptions from sales tax apply in certain situations, but they may be of limited import to art collectors. For example, sales tax generally does not apply to tangible personal property purchased for resale, but this exemption usually requires an intent to immediately resell, which is inconsistent with a purchase of artwork for a collection.[69] A more relevant exemption is for sales of "casual" or "occasional" sales of property, which could apply to an occasional sale of artwork by a collector (not through a dealer) who is not regularly engaged in the business of retail art sales. However, in California the sale of three or more pieces of art in a 12-month period renders the exemption inapplicable, and in New York the exemption is so limited in dollar amount that it would not practically apply to a single sale of fine art.[70]

[64] Elizabeth Carrott Minnigh and David E. Stutzman, *Planning for Authors, Musicians, Artists, and Collectors* (BNA Portfolio 815-3rd), VII.C.2. Only three states completely lack a sales tax—Delaware, New Hampshire and Oregon. Alaska and Montana do not have a statewide sales tax but allow localities to charge sales tax. Most states have a statewide sales tax with localities imposing their own local tax in addition. Id. Sellers generally charge sales tax to the purchaser so that it is a buyer cost, but are usually responsible for remitting sales tax even if they fail to collect from the purchaser. Id.

[65] *Quill Corp. v. North Dakota*, 504 US 298 (1992), overruled by *South Dakota v. Wayfair Inc.*, 585 US. __(2018),

[66] Elizabeth Carrott Minnigh and David E. Stutzman, *Planning for Authors, Musicians, Artists, and Collectors* (BNA Portfolio 815-3rd), VIII.B.5.a.

[67] Margaret Carrigan, "The tax man cometh: new laws on sales tax pose problems for US art dealers," *The Art Newspaper*, December 5, 2018, *theartnewspaper.com/2018/12/05/the-tax-man-cometh-new-laws-on-sales-tax-pose-problems-for-us-art-dealers*.

[68] "COVID-19 Impact Survey of US Galleries," Art Dealers Association of America, July 20, 2021, *artdealers.org/sites/default/files/ADAA%20Impact%20Survey%20Release_2021%20%2BREPORT.pdf*.

[69] *See, e.g., Matter of the Petition of P-H Fine Arts, Ltd.*, NY Tax Appeals Tribunal, October 13, 1994, confirmed 227 AD 2d 683 (3d Dep't 1996) (petitioner's purchase of artwork did not qualify for the resale exclusion because petitioner displayed the artwork before reselling it).

[70] Cal. Code Reg., Tit. 18, § 1595; NY Tax Bulletin ST-807 (TB-ST-807) (only first $600 is exempt).

Use tax

In addition to a sales tax, many states impose a complementary use tax, which is generally measured in the same manner as sales tax, i.e., the sales price of the property.[71] As a general rule, the use tax only applies to purchases from out-of-state sellers that were not required to collect sales tax on that sale, including purchases from foreign jurisdictions. The principal purpose of the use tax is to prevent the evasion of the sales tax on the purchases of tangible personal property made in another jurisdiction where either no sales tax was imposed or the applicable tax rate was lower.[72] With use tax, the tax due is from the buyer, not the seller. As a result, it is more difficult for states to enforce use tax compliance than sales tax compliance.[73]

Use tax may apply to collectors who transport their artwork. A collector with multiple residences may owe use tax when they move a work of art from one home to another, or when they decide to change domicile. For example, in New York, use tax may apply to individuals who are domiciled in another state if they maintain a place of abode in New York and hold their artwork in their New York residence, or even loan artwork to a New York museum.[74]

To delay the imposition of use tax liability, some collectors may purchase fine art and arrange to have it shipped directly to a state with no sales or use tax, to be stored there until the collector decides to ship it to a new location. Businesses have developed around this strategy—Delaware now has a number of secure, temperature- and humidity-controlled storage facilities where collectors can store their artwork. These facilities can be useful for collectors who cannot decide where to hang their art and need a temporary holding place.[75] If the artwork is brought into a state with a use tax, the tax would generally apply at the time of transfer to the use tax state, as discussed above. Certain exceptions apply, however. For example, California does not impose use tax on artwork that is purchased out of state and displayed in a state that does not impose sales or use tax for more than 90 days. This is because California exempts use tax on items purchased with the intention of first using them outside the state, and there is a presumption that such was the purchaser's intention if the property is initially used out of state for more than 90 days after purchase.[76] It has been reported that some California collectors have taken advantage of this rule by purchasing artwork and first loaning it to a museum in Oregon, which has no sales or use tax, before ultimately bringing it to California as its final destination. This structure has not yet been the subject of any cases and may be subject to challenge. New York does not have a similar rule.[77]

[71] However, in some states use tax is based on the fair market value of the property when brought into the use tax state.
[72] Elizabeth Carrott Minnigh and David E. Stutzman, *Planning for Authors, Musicians, Artists, and Collectors* (BNA Portfolio 815-3rd), VIII.B.5.b.
[73] US Gov't Accountability Office, Testimony before the Committee on Finance, US Senate, Remote Sales Tax: Initial observations on Effects of States' Expanded Authority, Statement of James R. McTigue, Jr. (June 14, 2022) (page 1, note 5, citing Minnesota report that observed only 1% to 2% of income tax returns included use taxes).
[74] Elizabeth Carrott Minnigh and David E. Stutzman, *Planning for Authors, Musicians, Artists, and Collectors* (BNA Portfolio 815-3rd), VIII.B.5.b(1).
[75] Eileen Kinsella, "New Delaware Freeport Offers New York Collectors an Art Tax Haven Close to Home," Artnet, October 16, 2015, *news.artnet.com/market/delaware-freeport-tax-haven-341366*, This article points out that how the artwork is shipped may impact the application of sales or use tax.
[76] Cal. Code Reg., tit. 18, § 1620(b)(3).
[77] Elizabeth Carrott Minnigh and David E. Stutzman, *Planning for Authors, Musicians, Artists, and Collectors* (BNA Portfolio 815-3rd), VIII.B.5.b.(2) (citing Graham Bowley and Patricia Cohen, "Buyers Find Tax Break on Art: Let it Hang Awhile in Oregon," *New York Times*, April 12, 2014, p. A1).

Gift transactions

While sales and use tax are primarily relevant for sales or purchases of artwork for consideration, in some states they may apply to certain gift transactions as well. For example, New York treats a grantor trust as a separate taxpayer from the grantor for sales and use tax purposes. As a result, the New York Department of Taxation and Finance has taken the position that a transfer of tangible personal property from a collector to the collector's grantor trust is subject to New York sales tax to the extent that the transfer is made for consideration.[78] The Department has also taken the position that a substitution by the grantor of tangible personal property for other property of value within a grantor trust was subject to New York sales tax based on the value of the substituted property.[79]

Under these rules, a pure gift transfer of unencumbered artwork from a collector to their grantor trust should not be subject to New York sales or use tax because it would lack consideration. However, if the artwork were subject to any debt, New York would appear to impose sales tax based on the amount of the assumed liability since it considers the assumption of liability to be consideration for sales and use tax purposes.[80]

Theft, worthlessness and abandonment of artwork

If a taxpayer holds an asset for investment and the asset is stolen, or becomes worthless or is abandoned, the taxpayer may be entitled to an ordinary loss deduction.[81] This ordinary deduction is available in the case of theft of artwork not compensated by insurance and may play a role in a collector's determination of how much insurance to purchase to cover certain pieces. The worthlessness and abandonment deductions could also be available to a taxpayer holding worthless artwork or a taxpayer who abandons artwork, but only if the taxpayer is holding the artwork for investment rather than for personal use. In addition, the transaction must be "closed" for the worthlessness deduction to apply (i.e., an identifiable event must demonstrate worthlessness). Similarly, for the abandonment deduction to apply, the taxpayer must demonstrate evidence of having fully abandoned the asset.[82]

[78] New York TSB-A-99(22)S (April 8, 1999).
[79] New York TSB-A-14(6)S (January 29, 2014).
[80] Id.; New York TSB-A-99(22)S (April 8, 1999).
[81] IRC §165(a). Boris Bittker and Lawrence Lokken, *Federal Taxation of Income, Estates and Gifts*, Chapter 25.
[82] Id.; IRC § 165(c)(2). In addition, the worthless and/or abandonment deductions come within the category of miscellaneous itemized deductions, which are suspended for taxable years 2018 through 2025. IRC § 67(g).

Non-fungible tokens

A non-fungible token (NFT) is a unique digital code that contains certain information. Like virtual currency, an NFT is created, stored and transferred on a blockchain network. It has no physical existence itself, but it generally denotes digital ownership of a piece of media, such as a work of art, song or video of a sporting moment. An NFT is non-fungible because it is distinct from every other NFT and non-divisible.[83]

Collectible status

The IRS treats NFTs as property.[84] A special long-term capital gains rate of 28% applies to gains from sales of artwork or other collectibles held for more than one year. Until 2023, it was unclear whether NFTs would be considered collectibles for purposes of applying this special rate. However, in March 2023, the IRS indicated that Treasury would issue regulations taking a "look-through" approach to determining whether an NFT was a collectible. This approach requires looking through the NFT to the asset underlying the NFT. For example, an NFT that certifies ownership of a work of art like a gem or an oil painting would constitute a collectible. The IRS is still considering whether a digital file that contains an image should be considered a work of art; if so, then any NFT whose associated asset is itself a digital file would be considered a collectible under the look-through approach.[85]

Charitable donations of NFTs

A collector who donates artwork to a charitable organization may only take a deduction equal to the fair market value of the property if the collector obtains a qualified appraisal.[86] A qualified appraisal must be completed by a qualified appraiser, defined as an individual with verifiable education and experience in valuing the type of property for which the appraisal is performed. This education and experience is evidenced by either: (1) an appraisal designation from a recognized professional appraiser organization based on competency in valuing the relevant type of property; or (2) (a) completed college or professional coursework relevant to the property valued; and (b) at least two years of experience in valuing the type of property being appraised.[87] Since the technology and marketplace for digital assets are so new, it may be difficult to identify an individual who would meet these requirements with respect to NFTs.

Moreover, donations of tangible personal property to a charity are subject to the additional requirement that the property must relate to the charity's exempt purpose in order for the donor to obtain an income tax deduction equal to the fair market value of the property. It is not yet clear whether the "related use" requirement would apply to digital assets. However, given the look-through approach that the IRS is taking with respect to the collectibles analysis, it is possible that the IRS would look through NFTs to the associated asset for the exempt purpose analysis as well.

Worthless or abandoned NFTs

As discussed above, the Internal Revenue Code permits an income tax deduction for an investment that becomes worthless or is abandoned during a taxable year. While the IRS has not yet addressed this issue in the context of NFTs, it has addressed it in the case of cryptocurrency that lost significant value during a taxable year in a chief counsel's memo. In the memo, the IRS reiterated that the asset must become completely worthless during the year in order for the worthlessness deduction to be available. Alternatively, the taxpayer must show evidence of abandonment in order to claim an abandonment deduction.[88] Presumably similar principles would apply to a taxpayer who holds an NFT as an investment that has declined in value.

[83] Robyn Conti, "What Is An NFT? Non-Fungible Tokens Explained," *Forbes*, March 17, 2023, *forbes.com/advisor/investing/cryptocurrency/nft-non-fungible-token*.

[84] IRS Notice 2014-21, Q&A 1-2. The majority of the official IRS guidance regarding digital assets addresses virtual currencies, not NFTs. This guidance takes the position that virtual currency is treated as property for income tax purposes, rather than as a traditional currency. Although there is no published guidance officially taking the position that NFTs are property, the IRS's first notice regarding NFTs implies that they are property, and the IRS website states that it views all digital assets, including NFTs, as property. "Digital Assets," Internal Revenue Service, *irs.gov/businesses/small-businesses-self-employed/digital-assets*.

[85] IRS Notice 2023-27.

[86] Treas. Reg. § 170A-17(b)(1).

[87] IRC §§ 170(f)(11)(E)(i)-(ii); Treas. Reg. § 1.170A-17(b)(2).

[88] CCA 202302011 (January 10, 2023).

Conclusion

At the heart of most great collections are individuals who have exercised their simple and direct love for art by seeking to be near it, to live with it, to preserve it and to share it with others. Over the course of doing so, they have likely forged a deep knowledge of the works they own, developed a sprawling network of like-minded and influential people who have helped them along the way, and accumulated a bank of trusted resources to guide them through the overlapping areas of expertise required. This publication seeks to both become one of those informative resources and to encourage engagement between our collecting clients, their wealth management team, and the specialists who can support their efforts in building meaningful and impactful collections.

Collections of consequence, composed of truly one-of-a-kind historical objects and directed by individuals with unique goals and motivations, will always be distinctive from one another. As such, the guidance in this text will be best exercised through active planning with the experts who can craft their advice to the needs of a collector and their ambitions.

The three centers of expertise at UBS that authored these articles carry enormous experience directly advising clients on the particulars of their collections, and how to thoughtfully build, manage and activate them. Our capability range includes Art Advisory—to guide collectors through many stages of developing a collection; Family Advisory and Philanthropy Services—to develop the philanthropic potential around collecting; and Advanced Planning—to strategically plan for the transitional moments in a collection. To partner with our teams for your collecting goals, please contact your UBS Financial Advisor.

About the UBS Art Collection

With over 30,000 artworks by influential artists of our time, the UBS Art Collection is one of the most significant corporate collections worldwide. UBS has been collecting contemporary art since the 1960s. It is a passion that we share with a large global community of clients. The Collection's guiding mission is to collaborate with and collect work by the most significant artists of our time. These works, displayed in UBS offices globally and in the UBS Art Gallery in New York, inspire thought and conversations about significant issues that affect our world. UBS also actively lends works to major art museums and cultural institutions for public exhibitions.

A select number of images featured in this publication are from the UBS Art Collection as cited.

About the UBS Collectors Circle

The Collectors Circle brings together clients from around the world who are passionate about art and collectibles (e.g., cars, watches and wines). Members can share their initiatives as well as receive the latest developments and trends for collectors through articles, videos, reports, webinars and webcasts.

Author biographies

Matthew Newton
Director
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Matthew is a Director and Art Advisory Specialist in the Family Office Solutions team within Private Wealth Management. The Family Office Solutions (FOS) team holistically services $100mm+ clients and family offices in partnership with Private Wealth Advisors. In this role, Matthew works with clients and their advisors as a thought partner to provide guidance, assess their needs and offer solutions through a suite of services focused on art collecting, collection management, art legacy, art historical education, due diligence processes and risk management related to collecting. FOS Art Advisory seeks to assist ultra high net worth clients with bespoke and custom advice to build and maintain exceptional art collections in context of their overall wealth management. Additionally, Matthew supports Private Wealth Advisors with customized art and collecting educational initiatives aimed at helping advisors connect meaningfully with clients in their passion asset.

Before joining UBS, Matthew developed a decade-long career in the commercial fine art gallery space, culminating as Associate Director at Michael Rosenfeld Gallery LLC, New York where, along with the gallery owners, he helped position the gallery as a distinguished top leader among fine art institutions. In that role, he provided thought leadership, trusted perspective and personalized practical guidance supporting prominent collections. He also contributed directly to the curatorial vision of gallery exhibitions, directed the global art fair program, managed strategic initiatives and special projects including large-scale public commissions, artist estate management, and ambitious museum lending efforts. His integrated art world experiences provide an array of resources and perspectives in service of comprehensive collecting guidance.

Throughout his career, Matthew has fostered ongoing meaningful relationships with leaders across the art market, exhibiting institutions, art fairs, vendor networks and museums with an overall objective of helping collectors build and manage sophisticated, lasting and personally meaningful collections. Originally from rural Georgia, before his career in the art world, Matthew began as an art educator and still today carries a passion for sharing the enjoyment of great art.

Matthew graduated magna cum laude from the University of Georgia with a dual B.F.A. in art and art education. He also received his M.F.A. from Hunter College of The City University of New York.

Nicole T. Sebastian, CAP®
Executive Director
Senior Strategist
Family Advisory and Philanthropy Services
Family Office Solutions

In January 2019, Nicole joined the newly formed Family Office Solutions (FOS) team within UBS Private Wealth Management, serving as a Senior Strategist representing Family Advisory and Philanthropy Services Americas. Nicole works closely with Advisors in Private Wealth Management, where FOS delivers dedicated and comprehensive services to ultra high net worth clients.

In this role, Nicole works with families on understanding values and philanthropic intent in the context of family wealth. She provides advice on family wealth education, communication and decision-making, multigenerational wealth transitions, and family governance as well as on charitable vehicles and building and enhancing philanthropic legacies. She also helps clients to be strategic and impactful with their philanthropic giving.

Nicole joined UBS in 2014 to establish and lead the UBS Optimus Foundation presence in the US, a global network that supports programs focused on the potential to be transformative, scalable and sustainable in the areas of health, education and child protection. Under her leadership, the Foundation platform became available to all clients and employees of UBS Financial Services Inc., and this offering now serves as a true differentiator and is a core component in delivering the firm.

Nicole has over two decades of experience in the nonprofit, philanthropic and corporate sectors, and brings a wealth of knowledge in nonprofit management, corporate and nonprofit governance, fundraising, performance assessment, leadership advisory services and policy research.

Previously, Nicole held roles with Heidrick & Struggles, Robin Hood Foundation, VCG Governance Matters, French-American Chamber of Commerce, Saint-Gobain Desjonquères, UNICEF and UNDP. She has served as an Adjunct Professor at Columbia University, teaching a graduate-level Strategic Management course, and currently serves as an Adjunct Professor and Advisor for NYU Stern's Board Fellows Program, a year-long experiential class offered to second-year M.B.A. candidates.

Nicole received her M.P.A. from Columbia University and B.A. from SUNY Geneseo. She is a founding member of the Young Professionals Committee of Susan G. Komen for the Cure and previously served as a Board member of the Women's Executive Circle of New York (WECNY). Nicole holds the Series 7 and 63 securities licenses, and is a Chartered Advisor in Philanthropy® (CAP®).

Debra G. Phares, CAP®
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As part of the UBS Family Advisory and Philanthropy Services team, Debra serves as a thought partner to advisors and their client families on wealth transition, family governance and philanthropy as families seek guidance on cohesive dialogue between generations to perpetuate their legacy.

Prior to joining UBS Financial Services Inc. in 2020, Debra was with Bank of America Private Bank where she spent eight years as a Senior Vice President and Philanthropic Director managing philanthropy services for the South Central region of the US. Debra worked with high net worth and ultra high net worth individuals and families, private foundations and nonprofit organizations delivering best practices in charitable giving and philanthropy, including directing grantmaking for private foundations and charitable trusts for which the Bank serves as Trustee or co-Trustee. Before Bank of America, Debra held various leadership roles in nonprofit management, beginning her career working in the museum industry, joining the Dallas Museum of Art in 1994. Following her career in the arts, Debra worked for the Communities Foundation of Texas and Parish Episcopal School.

Debra currently serves as a member of the Development Committee of The Senior Source of Dallas, whose mission is to enhance the quality of life and empower all older adults in Dallas to thrive. Debra previously served as a Vice President of the Board of the Aaron Family Jewish Community Center.

Debra is a graduate of The University of Texas at Austin with a B.A. in art history. She holds the Chartered Advisor in Philanthropy® designation from the American College of Financial Services, and also holds the Series 7 and 63 securities licenses. Debra lives in Dallas, Texas with her two sons and her mini dachshund.

As a Senior Strategist with Family Advisory and Philanthropy Services, Julie works with families on understanding money, values and philanthropic intent in the family wealth context and the dynamic overlap of five types of capital—human capital, intellectual capital, social capital, foundational capital and financial capital. Family and Philanthropy Advisory is a thought partner to advisors and their exceptional client families on wealth transition, family governance and philanthropy as families seek guidance on cohesive dialogue between generations to perpetuate their legacy.

Prior to joining UBS Financial Services Inc. in 2018, Julie was with Foundation Source, a provider of comprehensive support services for private foundations for nearly a decade. While there, she was responsible for understanding the needs and identifying philanthropic solutions for ultra high net worth clients and the Private Wealth Advisors who serve them. Julie worked with hundreds of clients to think about the impact of their philanthropy on their families and communities. Before Foundation Source, Julie worked for a boutique consulting firm that specialized in corporate philanthropy, and spent several years in business development for *Texas Monthly* and *New York Magazine*.

Julie graduated from the University of Connecticut with a B.S. in marketing and holds a Fellow in Charitable Estate Planning from the Charitable Estate Planning Institute. She holds the Chartered Advisor in Philanthropy® designation from the American College of Financial Services, and also holds the Series 7 and 63 securities licenses. She is an active volunteer with many local community organizations, and lives in Stamford, CT with her husband and two sons.

David Leibell
Executive Director
Senior Wealth Strategist
Advanced Planning
Family Office Solutions

David serves as a Senior Wealth Strategist, splitting his time between New York and Stamford. David focuses on comprehensive strategies to assist UBS clients with their complex financial needs such as preservation, transfer and management of wealth. He serves as an internal resource for UBS clients on all issues related to tax, estate planning, philanthropy, family business succession and wealth planning.

Prior to joining UBS in 2013, David worked at Wiggin and Dana where he was a partner in the Private Client Services Department focused on representing wealthy individuals and families, along with business succession and charitable planning. Prior to Wiggin and Dana, he was a partner in the Private Clients Group at Cummings & Lockwood.

David has authored over one hundred articles on charitable, estate and tax planning and given several hundred lectures and webinars to lawyer and non-lawyer audiences throughout the United States. He serves as the Chairperson of the Family Business Committee for *Trusts and Estates Magazine* and was previously the Chairperson of the Charitable Giving Committee for *Trusts and Estates Magazine* for eight years.

After receiving a B.A. from Trinity College, David continued to earn a J.D. from Fordham Law School and an LL.M. in taxation from New York University.

Lora Cicconi
Executive Director
Senior Wealth Strategist
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Lora works with ultra high net worth clients to help coordinate their income tax planning. She has experience with the federal, state and cross-border income tax aspects of acquisitions, financings, equity grants and buyouts. Lora is also a Specialist for the Family Office Solutions team, which holistically serves $100 million+ clients and family offices in partnership with Private Wealth Advisors.

Prior to joining UBS, Lora was Senior Vice President, Tax, at Lionsgate Entertainment. Previously, she was a practicing tax attorney at the law firms of Greenberg Glusker LLP and Gibson Dunn LLP.

Lora received her B.A. in economics from Stanford University. She received her J.D., Order of the Coif, from UCLA Law School, where she was a member of the *UCLA Law Review*.

Jacqueline Denton
Director
Associate Wealth Strategist
Advanced Planning Group

Jacqueline works closely with Senior Wealth Strategists and Advisors to coordinate investment, estate and tax planning, and philanthropic goals for ultra high net worth clients of UBS. She focuses on comprehensive financial planning to assist clients with their complex financial needs such as preservation, transfer and management of wealth. Jacqueline also reviews clients' existing estate planning documents to ensure that their planning accurately reflects the family's philosophy, needs and objectives.

Jacqueline joined UBS in 2015 and served as Assistant General Counsel before joining the Advanced Planning Group in 2021. In her role as Assistant General Counsel, she supported the UBS Private Wealth and International Divisions of the firm. Prior to joining UBS, Jacqueline was a shareholder with the law firm Grant, Fridkin, Pearson, P.A. in Naples, Florida, where she helped individuals and families achieve wealth transfer goals while minimizing estate, gift, income and generation-skipping transfer taxes.

Jacqueline received her LL.M. in taxation from the University of Florida, her J.D. from Cumberland School of Law and her B.S. from Indiana University.

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