

A Trust and Estate Lawyer's View

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When Bill Helfand and I first discussed my presentation today he asked that I speak as a collector, but also as an attorney representing people who owned books, prints, and works on paper, and what had changed since September 2008, both in terms of my own collecting experience and in terms of my clients' experiences and expectations about the values of their collections and the eventual disposition of those collections.

In considering the subject from the standpoint of a collector, and doing some research among Grolier publications, I realized that I am not qualified to speak to you today, or any day. Why not? Well, in a 1924 Grolier publication, *Three Essays*, by Augustine Birrell (the sixth and last book of the Club's Printers' Series), the author had this to say about the authority of a collector to speak about his collection:

"Libraries"—and he is speaking of private libraries—"are not made; they grow. Your first two thousand volumes present no difficulty and cost astonishingly little money. Given 400 pounds and five years, an ordinary man can in the ordinary course, without undue haste or putting any pressure upon his taste, surround himself with this number of books, all in his own language, and thenceforward have at least one place in the world in which it is possible to be happy. But pride is still out of the question. To be proud of having two thousand books would be absurd. You might as well be proud of having two topcoats. After your first two thousand, difficulty begins, but until you have ten thousand volumes the less you say about your library the better. Then you may begin to speak."

Accordingly, thank you for inviting me today. This ends my remarks as a collector. But not so fast—I do have some general observations about other collectors in this time of troubles, and a few remarks as an attorney; just a few.

The most immediate impact of the troubles came quickly, and to my wife, Stuart. A bookseller e-mailed her last spring and offered her two works for surprisingly low prices. She quickly expressed an interest, photos of the works were sent, and one of them she purchased immediately for about thirty percent to forty percent of what she believed the items would have sold for a year earlier. The dealer was quite frank about it—the works had been in a private collection of a client who needed to sell a few items quickly. The dealer knew of Stuart's collection and gave her an opportunity to buy them, but for cash immediately, no terms. At that price it was a done deal. The work arrived and Stuart was thrilled to own it. Hard times, indeed, and Stuart was an opportunistic buyer from a stressed seller, so here was an example in hard times of an object coming on the market that would not have been on the market except for the economic situation. Unfortunately, no dealers made such an offer to me.

I have also noted a significant decline in the prices of works which are not by "hot authors." Consider the American authors of the late nineteenth and early twentieth centuries. While some of their works have been kept alive by the Library of America, the general public and collectors have shunned them. Their prices were kept up a bit because of the value of their publishers' bindings, or the illustrations. But now, in hard times, you can find their works on-line, or in dealers' inventories at virtually second-hand book prices: Howells, Holmes, Garland, London, Lewis, Riley, Dunbar, Cable, Frederick, Jewett, Wilkes Freeman, to name a few. Flight to quality some would say. But when the prices get low enough, they sell. Savvy dealers are pointing this out, and collectors may be getting interested, but, not having a library of 10,000 volumes, I am not qualified to speak on collecting, so I must move on.

I do have several observations as a lawyer representing individual clients and their estates.

The serious decline in the value of stocks, bonds and other assets during this recession has had a substantial impact on valuation issues affecting books, prints and other fine arts. Here's how:

When you die, your assets are valued as of the date of your death for federal estate tax purposes. If an estate tax is due, your executors also have an election to value those assets on the alternate valuation date, which is six months after death. The federal estate tax return must be filed nine months after death and the tax, if any, must be paid then. The executors have an automatic right to file for an extension of time to file the return, which, if the election is made, must be filed six months later, or fifteen months from the date of death. You can see where I am going.

In our office we had two estates with significant works of art, books, furniture and silver. In one estate the date of death was April 2008 and the alternate valuation date was October 2008, and the return was due in January 2009. In the other estate the date of death was in December 2008 and the alternate valuation date was in June 2009, and the return is due this month.

The executors in those estates recognized that they had serious valuation issues on the books and works of art. They and their appraisers felt intuitively that the value of those works had declined in value after September 2008. In the first instance where the date of death was before September 2008, the appraisals were relatively easy, because the art and book market was fairly stable and there were plenty of comparable prices around. But what about their alternate valuation date of October 2008? Had the market in the collectibles already begun its decline? Could the appraisers demonstrate that decline through comparables and would they be willing to sign an affidavit of appraisal showing through their valuations that a decline in value had already taken place? Now I have to tell you that in this estate they could not do that, but only because there was no estate tax due to the marital deduction, and of course they wanted higher values so that there would be reduced capital gains taxes if the items were sold at a later date.

But what if there had been enormous estate taxes due? The government would have taken the position that the assets had not yet really declined in value, that there were no comparables to demonstrate it, and that the executors could not use later sales as proof of the decline. The executors and their appraisers would have been faced with a situation where they would have had to take the position that the assets were worth less, because otherwise they would be faced with significant losses when they eventually sold them at auction if in fact the market had declined. They were between a rock and a hard place, and you can bet your life the government would have played hardball here.

Well, you can say, so what? I am alive, so my estate is not faced with two significantly different valuation dates. What's the big deal?

The big deal is: How do you value the books or works of art if you die soon, or make a gift either to an individual or to charity? If you die, your estate may want a higher or lower value, depending on the facts as I discussed a moment ago. Can you establish to the satisfaction of the Internal Revenue Service that there has been an erosion in value of those assets, or a decline in the value of books as an asset?

What about lifetime transfers of books or art? How about gifts? Let's consider first gifts to individuals—a family member other than a spouse. We have a client right now who wants to make a significant gift of art to his children. Good timing, yes, because the works must be appraised and the appraisers may take the position that the market for these particular works has declined since the stock market declined, perhaps by as much as thirty-five percent. Will those values hold up for gift tax purposes? Can the appraisers find comparable sales figures? I don't know, and because some of the works are significant, the art panel in Washington will probably get the question if the gift is made and a return filed. And interestingly, here there is no tax to be paid because the donors have not used any of their federal gift tax exemption of \$1,000,000. However, they want those gifts valued at the lowest possible amount in order to preserve the remaining exemption for future gifts.

So, it might be a good time to make gifts of collectibles to individuals if you believe and can substantiate that the market value has declined for those items. And that is particularly the case if you believe the value of those items will rebound at a later date. Lock in the lower value now.

Similar problems arise with gifts to charity, but here you want just the opposite result, because you want a large deduction. So if you had insured the works based on fair market value appraisals fairly recently, you may face resistance from the government if you try to use that value for your deduction, and you will certainly face resistance if you try to show a significant increase in value in the last year or so, unless you have comparable sales figures to support you.

There are some other problems related to the September 2008 financial situation. In our office we find that because of the uncertainty in the valuation of fine art, the government is simply dragging its feet on valuation questions. If you

have filed a gift tax return or an estate tax return with any work of art valued at more than \$20,000, and if the return is audited, the IRS will send the appraisals to the art panel, which is charged with setting a fair market price for valuation purposes. The art panel has really slowed down its work, and the government is now, we find, taking much longer to negotiate the values, or to close returns with valuation issues. In one case in our office, the art panel has now had a valuation issue before it for over a year, and still no ruling.

The art panel is not supposed to know whether the valuation is for estate tax purposes (where the taxpayers usually want a lower valuation) or for charitable gift purposes (where the taxpayers usually want a higher valuation). But anecdotal evidence suggests that in matters relating to estates in the last year they have raised the valuations, and for charitable gifts, just the opposite. Coincidence?

In summary, with the markets in fine art in an uncertain period, you are going to risk an audit with any significant gift of valuable books or in estates containing such items where tax returns are required to be filed.

This might be a very good time to resolve issues of valuation by having your insurance adjusted to reflect lower values. That will necessitate an appraisal, of course, and it will not be binding on the Internal Revenue Service. But if a gift follows soon thereafter, or if you die, you have a current value to work with, not one fixed when the markets were at their height. The danger with this, of course, is that if the markets rebound you are under-insured.

Finally, the timing of the sale of books and other works of art has been significantly affected by the recession. Many sales have been delayed where sellers had some flexibility. Some sellers have not had the luxury of waiting for improved market conditions.

There are no easy answers here. But, through careful planning and discussions with your appraiser, accountant and lawyer, you can be creative in your planning and the disposition of these assets.