

How to Plan for the Best Pieces in Your Collection

by Michael Mendelsohn

The important pieces in your collection are generally your finest once-in-a-lifetime purchases. Planning for the disposition of these pieces usually involves different considerations than the decisions required for other items. It's necessary to document provenance and determine the current value of these pieces with an updated appraisal. Additionally, if you have children, you also need to talk with them to determine if they want certain pieces or if they prefer the cash: You need to be clear about each others' objectives.

If the Art Goes to the Children

If a child indicates an interest in an antique rather than the proceeds from its sale, you need to work with your advisory team to create financial mechanisms to provide a source of funds to pay the inheritance and gift taxes involved. The most common means is with an Irrevocable Life Insurance Trust (which is simply an insurance policy). When properly set up by your attorney, the proceeds can go into the trust, income- and estate tax-free. Your children are made the beneficiaries and — with the proceeds — will be able to buy the object from the estate. The trust will also provide cash for children who prefer that option. This kind of planning ensures equitable distribution and, most importantly, prevents future family art wars.

Creating your Legacy

Another approach is to gift pieces to a museum, which results in a charitable deduction. The sticky wicket here is that taxpayers are limited in the amount they can deduct annually for gifts to charity and you might not be able to take full advantage of the deduction in one year. Fractional gifting allows you to donate a percentage rather than the entire work of art to a museum or other “related use” institution. Assuming the charity can actually use and display the work (known as the “related use” rule) you will receive an income tax deduc-

tion equal to the fair market value of the donated share (a qualified appraisal is required).¹ If you donate additional percentages in subsequent years and the value of the work has appreciated, the tax deduction will increase. This approach allows you to continue to enjoy the piece in your home for a portion of the year and take full advantage of the charitable tax deduction over a period of time. As we go to press, there is a bill in Congress that may place additional restrictions on fractional gifts.



Morris Hirshfield (1872–1945) *American Beauty*, 1942. Oil on canvas, 48 X 40 inches. For important art and objects, it is financially responsible to discuss and set in place a plan for your finest pieces.

Museum Without Walls

A museum without walls is a legal entity created to act as a lending library to museums all over the world. In situations where a collector has assembled a group of pieces that are worthy of a traveling exhibition, the collector can use this planning technique. The museum without walls concept allows the collector to advertise the availability of the items for exhibition and fundraising events, travel the world, and create

future family philanthropy. This is a particularly appropriate planning strategy for the best parts of collections where the items have more value as a collection than as individual pieces.

This planning strategy works through a private operating foundation (POF) created by your attorney. Once the POF is created, your best items, for exhibition purposes, are gifted to the foundation and you will receive a tax deduction for the gift.² The deduction is the equivalent of the fair market value of the dona-

tion, as long as the property fulfills the following obligations: it must satisfy the “related use” rule; have been owned by you for more than one year and was not a gift from the artist; and have been appraised by a qualified appraiser. The other parts of your collection can then be sold or gifted to create an endowment fund to help the foundation promote exhibitions and generate revenue for philanthropic purposes.

Through proper planning of your best pieces, you can not only ensure you pass on a legacy to your children, you can also generate a stream of income to help you grow and improve your collection. However, there are technical requirements to implementing these strategies, which your advisory team or art succession planner can help sort out.

All of these approaches require the assistance of legal and financial professionals. @

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¹ See Treas. Reg. §1.170A-13(c)(2) and (3) for more information.

² See IRS Publication 578 — Tax Information for Private Foundations.