Art through the ages

Sandrine Giroud explains how to pass an art collection to the next generation, without it becoming fragmented.

Whether a passion or an investment, art is forming an increasingly large part of private clients' portfolios. However, without adequate estate planning, collections built over years can be very quickly dismantled.

Dissension among heirs may cause the collection to be divided, thus reducing its overall value, or tear families apart. For instance, when Picasso died in 1973, he left a collection worth hundreds of millions of dollars, but no will. As a result, his widow and progeny (both legitimate and illegitimate) battled in court for years over the distribution of thousands of his paintings, sculptures and drawings.

Sometimes, personal taste comes into play, when parents' collections do not hold the same appeal for their children. In other cases, neglected tax-payment issues may overwhelm the collector’s heirs, forcing them to sell part of the collection.

To avoid such unfortunate outcomes and ensure the harmonious transfer of a collection between generations, the following steps, from a Swiss law perspective, are worth considering.

COLLECTOR’S OBJECTIVES
The collector’s vision and objectives are at the core of any decision regarding the structuring of a collection. They may include preserving the collection’s unity, ensuring a regular income for surviving family members, contributing to an artist’s legacy or pursuing an exclusive philanthropic goal.

The collector’s objectives must be clear and unequivocal, yet sufficiently broad to ensure their adjustment over the course of time, specifying in particular whether the collection should be preserved in whole or in part, whether it is inalienable or not, and whether it can be expanded – and, if so, in which direction.

LEGAL PLANNING
From a legal standpoint, a collector needs to clarify two issues early: under which law their estate falls, and which legal structure is best suited to host the collection.

Applicable law
A collection is subject to the law governing the collector’s estate. This determines issues such as what belongs to the estate, who is entitled to it and the scope of this entitlement; who will meet the debts of the estate; and the legal remedies available. Under Swiss private international law, these rules may, within certain limits, be departed from by choosing a different law.

The extent of a collector's estate will also depend on the matrimonial property regime applicable to the marital community. To a certain extent, Swiss private international law allows spouses to determine the law governing their matrimonial property regime.

The disposal of one's estate remains subject to the matrimonial property regime and inheritance rules protecting direct family members – e.g. the division by
default of the property acquired by the spouses during their marriage, or forced heirship rules.

Swiss law provides different options to mitigate the impact of these rules, such as compensating the other spouse for their share of the collection; contractually choosing a different matrimonial property regime (e.g. separation of property); or structuring the distribution of an estate among the heirs according to the deceased’s wishes (e.g. in a succession contract, a will or by way of specific instructions concerning the division of the estate).

Legal structures
When holding an art collection, the main structuring options are to hold it in one’s own name; through a legal vehicle such as a company, trust or foundation; or to give it away to a charity or a museum. The advantages and disadvantages of each are briefly described below.

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Companies
A collector can structure ownership of the collection through a company (Swiss or foreign). Companies facilitate the passing of the collection to the next generation through the simple transfer of shares and thus protect the collection from the collector’s creditors. However, companies do not ensure the preservation of the collection, which remains exposed to inheritance disputes over shares. Also, as with any other legal vehicle, this structure incurs management costs.

Trusts
An art collection may also be structured through a trust which, although not provided for under Swiss law, is recognised under the Hague Convention of 1 July 1985 on the Law Applicable to Trusts and on Their Recognition. When settled into a trust, an art collection is generally protected from the collector’s creditors, and special instructions can be given for its management. But these benefits come at the price of transferring control of the collection to the trustee.

Foundations
Swiss foundations have evolved as one of the most popular legal structures for the long-term care of art collections. Established by the endowment of assets for a particular purpose, foundations can be created either for public or private purposes and are supervised by the state authority to which they are assigned. A collector can entrust their collection to an art foundation under the obligation to ensure the preservation and public display of the collection, its continuous expansion, or its loan and use to expand its influence.

In principle, the purpose of a foundation, as set out in its statutes, cannot be altered, save under very strict conditions – namely by the supervisory authority, at the founder’s request, or in accordance with their testamentary disposition. A foundation also ensures a certain degree of confidentiality, as its annual accounts and annual report to the supervisory authority are not available to the public.

Although structuring an art collection by way of a foundation implies the full transfer of ownership to the foundation, the collector can ensure the continuous involvement of family members by statutorily providing for their participation in the foundation’s board.

Donation to public museums
Museums, subject to their own charter, may accept artworks as gifts and thus offer a perennial resting place to an art collection. Collectors, however, need to be clear on the requirements they want to impose on the museum through covenants or conditions attached to the gifts. Special instructions can be given for storage and restoration, the preservation of the collection’s integrity, the display of the collection or some of its items, and the mention of the collector’s name.
FOCUS ON SWITZERLAND AND LIECHTENSTEIN ART COLLECTIONS

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While tax liability should never be the prime consideration when structuring an art collection, it should not be overlooked either. In fact, many families have been forced to part with inherited artworks because they were unable to meet the tax obligations triggered by the succession or by the reappraisal of their collection at a substantially higher value.

In Switzerland, individuals are taxed on their wealth at cantonal and municipal levels, and on their income at federal, cantonal and municipal levels. Accordingly, directly owned art collections are subject to cantonal and municipal wealth taxes, except for artworks used as decoration (as opposed to a mere financial investment). In principle, gains from the disposal of artworks are not taxed if they result from the free ordinary management of personal wealth and not from a business activity.

There is no federal tax for gifts and inheritance. Most cantons impose a tax on gifts and inheritance, save for transfers to direct family members, such as surviving spouses and children. In certain cantons, the payment of gift and inheritance taxes can be made through the transfer of cultural objects to the state (so-called ‘dation en paiement’). Gifts to the state or public interest institutions are deductible from federal tax up to 20 per cent of the donor’s annual taxable income. The same generally holds true for cantonal tax, although certain cantons provide for full tax deductions.

Public interest foundations (charities) whose purpose is to benefit the public at large are tax-exempt. Art foundations whose collections are primarily and irrevocably dedicated to public display qualify as such. Endowments and bequests to public interest institutions are also generally exempted from tax. By contrast, companies or private foundations are subject to income and capital taxes at varying rates, depending on the canton and municipality.

BEST PRACTICE

Thoughtful legal and tax planning must go hand in hand with careful management of practical issues. Here is a brief overview of the main actions to consider.

- Transition preparation: collectors should ponder whether and when to involve the next generation in the structuring of a collection, and consult external advisors who may be responsible for taking the legacy forward.
- Documentation: documentation is crucial for establishing ownership, authenticity and provenance. The more documented an artwork is, the greater its value and the less its exposure to possible legal disputes. Proper documentation should include proof of purchase, a fact sheet and photograph of each artwork, any publication about the artist or the artworks, import or export documents, personal notes and correspondence, insurance records and statements from prior owners.
- Valuation: liabilities arising under the rules of the matrimonial property regime, inheritance or tax law are all based on the valuation of the estate, as well as insurance coverage. A reliable valuation is therefore key to adequate planning.
- Funding: maintaining, storing and exhibiting a collection involve costs that need to be provided for. Holding an art collection through a legal vehicle incurs additional costs, to support the structure and remunerate the management team.
- Good governance: establishing an art governance structure composed of a family council and a curatorial board of art experts, which acts according to well-crafted governance documents (e.g. a mission statement, collection policy and due diligence procedures), is an effective way to prevent legal disputes.

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CONCLUSION

As Hippocrates stated: ‘Life is short, art long, opportunity fleeting, experience perilous, and decision difficult.’ Beyond the common notion of ‘art’, Hippocrates meant art as craft and technique. The art of creating a collection also yields to the brevity of a collector’s life. To ensure its safe and peaceful passage through time, an art collection requires special adjustments and careful planning, with a long-term perspective and a clear sense of the underlying purpose. Advanced discussions with family members and professionals increase the chances that a collector’s vision will carry on through the generations.

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