What's Fair about FAIR MARKET VALUE?
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Lela Hersh, ASA
TERMS AND DEFINITIONS
Professionals should be Knowledgeable about the Terminology they use
What is this definition?

______________________ is the price that property would sell for on the open market. It is the price that would be agreed on between a willing buyer and a willing seller, with neither being required to act, and both having reasonable knowledge of the relevant facts.
Current Market Value

Or

Fair Market Value
FAIR MARKET VALUE as defined by IRS

Section 1.170A-1 (c) (2) and Regulation §20.2031-1
FAIR MARKET VALUE

Fair Market Value is the price that property would sell for on the open market. It is the price that would be agreed on between a willing buyer and a willing seller, with neither being required to act, and both having reasonable knowledge of the relevant facts.”

Section 1.170A-1(c)(2) and IRS Regulation §20.2031-1
SHOULD — Expected sale
COULD — Ability to sell
WOULD — Hypothetical sale
Terminology

Insurance vs. Appraisal

**Insurance**
- Current Market Value
- Agreed Value
- Actual Cash Value

**Appraisal**
- Fair Market Value
- Marketable Cash Value
- Replacement Value
- Salvage and Scrap Value
- Forced and Orderly Liquidation
- Market Value
- Fair Value
So What is **Current Market Value?**

- Not an appraisal term – definitions vary
  - Market value or current market replacement cost
  - The amount of money an item would bring if sold on the current local market
  - The largest amount any buyer is currently willing to pay for a bond
  - The price the item would bring if it were offered for sale by a willing but not obligated seller and purchased by a willing but not obligated buyer
  - An insurance value that is often higher than Fair Market Value due to the insurance component
• Is the definition of Current Market Value in any of your insurance policies?

• May differ
  – Museum Policies
  – High-end Collectors’ Policies
  – Art Dealers’ Policies for Inventory
  – Homeowners’ Policies
Values in Collections Management Policies

• The Board of Trustees or the Executive Committee must approve the deaccessioning of any work of art with a current market value in excess of $50,000 (The Metropolitan Museum) [http://www.metmuseum.org/about-the-museum/collections-management-policy](http://www.metmuseum.org/about-the-museum/collections-management-policy)

• Deaccession proposals must be in writing and must address the following...Current market value or auction estimates (and a written appraisal for any object valued over $10,000) [http://thewalters.org/about/policy/deaccessions-policy.pdf](http://thewalters.org/about/policy/deaccessions-policy.pdf)
Marketplaces used to find values

Replacement Value is always found at the gallery retail market

Fair Market Value is always found on the auction market

True or False?
FALSE

- **Replacement Value** is found in the most relevant market

- **Fair Market Value** is found in the most common market
What Difference Does the Marketplace Make?

• RELEVANT MARKET
  – For Insurance purposes
    • The insured should receive enough money to become “whole” again
    • Replace a loss with an object of similar age, quality, origin, appearance and condition within a reasonable length of time in an appropriate and relevant market
What Difference Does the Marketplace Make?

- COMMON MARKET
  - Court rulings for IRS purposes
    - Fair Market Value is determined in the market in which the item is most commonly sold to the public
    - Price which will be paid by the ultimate consumer of the property
      - The ultimate consumer is the customer who does not hold the object for subsequent resale
Marketplaces

• Objects sell for different prices in different markets
• Value is determined by the particular market
Museums Receiving Copies of Charitable Contribution Appraisals

• The donee is not the “Intended User” of an appraisal that is completed for a donor.

• If a donee uses a Charitable Contribution appraisal they have received from a donor, and later the museum loans the work and uses that Fair Market Value, their remedy for a claim most likely will be limited.
However, appraisals are still wonderful documents for museums to have for their records!
Insurance Value ≠ Tax Deduction

Insurance Valuation
$40,000

Fair Market Value
$7,000
Insurance Valuations

Key focus for this type of appraisal

• How much would it cost this client to replace a property in a reasonably convenient manner with one of comparable quality within a reasonable amount of time?

• Also, what ancillary costs might need to be included? shipping? Art Advisor? Interior Designer?
Market Changes

Markets are always changing, and the changes are not consistent for all types of property.
“Casablanca” Piano
Considerable Market Change

$154,000 Auction Sale in 1988

$602,500 Auction Sale in 2012

Same “Casablanca” Piano
Considerable Market Change

Same set of Louis XV Giltwood Fauteuils

£91,750 Auction Sale in 2000

Unsold No bidders at £26,000 Auction sale in 2011

Christie’s
Considerable Market Change

Same pair of George III Pier Tables

£81,800 ($132,250)
Auction Sale in 2001

£58,850 ($95,950)
Auction Sale in 2011

Christie's
Auction Estimates

Sometimes auction estimates are deliberately low (to encourage bidding) and sometimes over optimistic (marketing purposes).
High Auction Estimate

$800,000 - $1.2M

Sold for

$602,500

Sotheby’s
High Auction Estimate
$100,000

Sold for
$12,000

Legendaryauctions.com
Low Auction Estimate
$3,000 - $5,000

Sold for $27,500
Low Auction Estimate
$100,000 - $150,000

Sold for $962,500

Sotheby’s
Explaining Fair Market Value to Museum Donors

- Different from Insurance Valuations
- Markets Can Change Dramatically
- Auction Estimates Are Not Evidence
Recognizing that Markets Change

IRS Publication 561 requires

“...an appraisal made not earlier than 60 days before the date of contribution of the appraised property...”
Auction Estimates Are Not Evidence

“At Sotheby’s Sale, Estimates Prove to Be Just Wild Guesses”

“... It was one of those days that make you wonder how experts find the courage to make any forecasts about auction prices.”

When Fair Market Value Seems Most Unfair
Explaining to Donor

Work may be sold (at retail) for more than Fair Market Value.

“Likewise, individuals may be shocked when an item appraised in a family member's estate is seen in a retail store with a price tag of multiple times the appraised value.”
Explaining to Donor’s Heirs

Collection sold at auction for nearly 5 times its auction estimate
Explaining to CPA

Correctly insured
$40,000

Fair Market Value
if donated
$7,000

Net Receipts
if sold at auction
$4,000
Alan Francisco
What does this information mean for registrars?
Because they are aware of the potential problems that can result from getting too involved in donor valuations, registrars are often uncomfortable providing more than minimal guidance.
• This is especially the case in natural history and science museums, and to some extent in history museums, where donations rarely involve the high valuations of art museum acquisitions.

• Staff in such institutions tend to focus on the intellectual or scientific value of collections to the greater exclusion of monetary considerations.
Topics for

The Future

NEXT EXIT
Lela Hersh
ASA
TWO
CASE STUDIES
Even Rich Heirs Deserve A Fair Shake From The IRS

Sonnabend Estate v. Internal Revenue Service

(Forbes)
Robert Rauschenberg
Canyon, 1959

Oil, pencil, paper, metal, photograph, fabric, wood, canvas, buttons, mirror, taxidermied eagle, cardboard, pillow, paint tube and other materials

81-3/4 x 70 x 24 inches

• The 1959 combine by Robert Rauschenberg titled *Canyon* included a taxidermied bald eagle head - a protected bird

• Acts that caused problems with ownership
  
  – **1940 Bald and Golden Eagle Protection Act**
    • Eagle was killed before 1940

  – **1918 Migratory Bird Treaty Act**
    • Criminal penalties for persons who “take, possess, sell, purchase, barter, offer to sell, purchase or barter, transport, export or import, at any time or any manner, any bald eagle . . . alive or dead, or any part, nest, or egg thereof”

*ArtNews, May, 2012*
• Ileana Sonnabend bought *Canyon* from her former husband’s gallery (Leo Castelli) in 1959, the same year the work was made and first exhibited

• In 1981, the Department of Fish & Wildlife became aware of the eagle carcass in *Canyon* and agents notified the Sonnabend Gallery that its ownership was restricted

• A special permit was received to retain possession, and then from 1982-2003 *Canyon* was on long-term loan to the Baltimore Museum of Art

• In 1998, during the loan process to the Guggenheim for the artist’s retrospective, Fish & Wildlife threatened to revoke the 1981 permit unless they were given proof of nonprofit status or evidence that the bird was killed and stuffed prior to 1940

• Rauschenberg sent a notarized declaration to the government that the eagle had been killed and stuffed by one of Teddy Roosevelt’s Rough Riders before 1940

• An export license was not granted, but Sonnabend was allowed to retain *Canyon* with the understanding that the artwork could never be sold but could be loaned to museums in the US and abroad as long as proper permits were obtained

In 2007 Ileana Sonnabend died leaving her estate to son and daughter Antonio Homem and Nina Sundell.

- Estate paid $471 million in federal and state estate taxes by selling works from the collection for an estimated $600 million.
- At the time, *Canyon* was on long-term loan to the Metropolitan Museum, New York.
- *Canyon* couldn’t be sold and the Estate wanted to donate it.
- In 2011, the IRS sent the Estate an unsigned draft report indicating a Fair Market Value of $15 million.
- After the Estate refused to pay, I.R.S. sent a formal Notice of Deficiency indicating that they had increased the Fair Market Value from $15 million to $65 million.

Why $65 Million?

Top price ever paid for a Rauschenberg at auction is $14.6 million

*Overdrive*, 1962
Oil and silkscreen ink on canvas
84 x 60 inches
Sold at Sotheby’s, NY
May 14, 2008

Artnet
Sale six months after Sonnabend death date
Art’s Sale Value? Zero
The Tax Bill? $29 Million

Sonnabend Estate submitted different appraisers and each gave the subject property a **Fair Market Value** of $0.

For the $65 million that the IRS stated *Canyon* was worth, it charged the Estate an additional $29.2 million in taxes and a $11.7 million “gross valuation misstatement” penalty.
Sell on the Black Market

• Statement from New York Art lawyer, Ralph Lerner regarding Joseph Bothwell, then the interim head of the IRS Art Advisory Panel
  – “He told me there could be a market for the work. For example, a recluse billionaire in China might want to buy it and hide it.”

ArtNews, May 2012
"The government is saying we want $35 million in tax but if you sell it to get the money we’ll put you in jail."

Forbes, February 23, 2012, Nathan Lerner, Art Lawyer quoted
Resolution

• I.R.S. dropped the tax assessment
• In exchange, the Sonnabend Family was required to donate the Rauschenberg to a museum
  – with no tax deduction claimed
• The Museum of Modern Art, New York received the painting
• No extra Estate taxes were imposed on the Sonnabend Family
Wynn Settles Insurance Suit With Lloyd's Over a Torn Picasso

Wynn v. Lloyd’s London
• In 1941 Victor and Sally Ganz, New York buys Picasso's *Le Rêve (The Dream)* for $7K
  – Le Rêve is a portrait of Picasso’s lover Marie-Thérèse Walter
• In 1997 Christie’s sells painting for $48.4 million
• In 2001 the Christie’s purchaser sells to Steve Wynn
Oops!

• In 2006 Wynn agrees to sell *Le Rêve* to hedge-fund billionaire Steven Cohen for $139 million
• Wynn accidentally puts his elbow through the painting, leaving a several-inch tear across Marie-Therese's left forearm
• Cohen backs out of the sale
• Wynn claims the damage with insurance
• *La Rêve* undergoes 3 months of restoration for a reportedly $90K
• Disagreements arise over the Loss of Value
• Wynn sues Lloyd's of London
• Settles for approximately $40 million
  – Wynn had reportedly had been seeking $54 million
• Wynn sells *Le Rêve* to Steven A. Cohen for $155 million
### Looking at the Numbers in Millions

<table>
<thead>
<tr>
<th>Year</th>
<th>Amount</th>
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<tbody>
<tr>
<td>2001 Wynn Private Treaty sale</td>
<td>60</td>
</tr>
<tr>
<td>2005 Listed on Insurance</td>
<td>95</td>
</tr>
<tr>
<td>2006 Cohen agreement to buy</td>
<td>139</td>
</tr>
<tr>
<td>2007 Loss in value received (@29%)</td>
<td>40</td>
</tr>
<tr>
<td>2012 Cohen Purchase (@11% over)</td>
<td>155</td>
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- **Total Wynn Received**: 195
  - 155 (Cohen) + 40 (Insurance)
- **Total Wynn net in just over a decade**: 135

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Estimated numbers from undisclosed sales reported throughout the Internet and other industry discussions.
No one ever said it was FAIR