

Anchin Alert

Anchin, Block & Anchin LLP
Accountants and Advisors

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The Art of Tax Planning - Part 2

This is the second installment of an article about tax as it applies to the unique subject of art. You can find the previous article [here](#).

Fine art is increasingly making headlines as record breaking auction prices steal the attention of collectors, hopeful artists, and art market enthusiasts. At the same time, the perception of a rising art market has brought fine art to the attention of investors around the world, who now consider it an alternative asset class to be evaluated alongside real estate, hedge funds and other investments. Many collectors have realized tremendous appreciation on their accumulation of emerging and contemporary art, and a select few artists are experiencing strong financial success from their creations. However, unlike traditional investments, fine art can be incredibly illiquid and difficult to manage. A highly appreciated art collection belonging to an art investor, or a body of work in the possession of a successful artist, can become a significant liability if not properly planned for prior to the owner's passing.

Gifts and Bequests to Charities

Charitable transfers are generally treated favorably in the Internal Revenue Code. Gifts to a charitable organization during life are deductible for gift tax and generally can also be used to reduce federal income taxes, in the form of an itemized deduction. For art collectors who purchased the items in their collection outright and give them to a qualified charity for a related use, the income tax deduction will be at the full fair market value of the artwork. This can be a tremendous boon for the successful collector whose collection has significantly appreciated in value, although there are limitations on how much of a charitable deduction can be taken in each taxable year and a five-year limit on carryovers of excess deductions.

At death, charitable bequests are allowed as a deduction from the taxable estate and therefore can reduce or eliminate the estate tax. This deduction is at the full fair market value, so including a charitable bequest in the will of an artist or art collector can be very beneficial toward preserving the value of other assets by reducing the estate taxes that would otherwise be paid.

However, although charitable transfers of highly appreciated art are treated favorably at death, artists face a peculiar problem during life: they cannot give their artworks to museums and charities while they are alive and realize the same benefits as art collectors. The Code is not friendly to artists in this respect. Although a charitable gift of art would not be subjected to gift tax, because an artist's work is self-created an artist cannot receive a full fair market value income tax deduction for work given to charity. Instead, only the cost of the artist's materials, if not already deducted as a business expense, can be deducted. Because a working artist likely already deducted the cost of canvasses, bronze, certificates of authenticity, or anything else that went into the work, the value to the artist of a charitable gift is usually zero. Giving the art to a friend or relative is not an option either, as the exception for self-created artworks also applies to gift recipients, such that the recipient also can only realize a charitable deduction equal to the cost of materials. These rules can be an impediment to philanthropic planning for a successful, charitably-minded artist.

For more information, please contact your Anchin Relationship Partner, Gary Castle or Michael Belfer, Co-Practice Leaders of Anchin's Art Specialty Group, at 212.840.3456.



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