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Passion assets: When "Possession is not nine-tenths of the law"

By **Lawrence M. Shindell**, J.D., chairman of ARIS Title Insurance Corporation, discusses the legal title risks impacting the global fine art and collectibles market

> TODAY'S ART MARKET TITLE RISKS RUN THE FULL GAMUT OF OWNERSHIP RISKS SEEN IN OTHER MARKETS

Fine art and other precious collectibles is the new asset class for alternative investment strategies for individual and institutional clients.

Due to limited experience generally with the "insider-based" art market, most financial advisors and their clients do not fully understand the existence of third-party ownership claims in this market. Clear legal ownership in the art world is very different from simple possession, and it is the linchpin to a client's ability to buy, sell, donate, transfer or otherwise enjoy their art or collectible.

It is not just about stolen art anymore. Today's art market title risks run the full gamut of ownership risks seen in other markets – from secret estate tax liens and undisclosed factional ownership interests to claw-back claims of consignors who are victims of financially faltering galleries. Witness the recent sale by the world's top gallery of a multi-million dollar artwork to European buyers in which the Metropolitan Museum of Art held a 30% gift interest; or the case of Sam Zell, who consigned several million-dollar artworks to a California dealer, who absconded with the proceeds and left Zell to seek ex gratia coverage from his homeowner's insurer and the insurer to reclaim the art from the marketplace.

A full discussion of what engenders the global art market's title risks requires a separate article. Suffice to say here, the art market title risks – which are rising in complexity and frequency as the art market matures – encompass any lien or encumbrance that infringes the would-be owner's title to the art or important collectible and stems from prior historical and contemporary theft, illegal export or import, sale by a party lacking legal authority to sell, creditor claims, bankruptcy claims or unpaid government income or estate taxes.

The U.S. Supreme Court's June 2011 decision in United States v. Jicarilla Apache Nation affirmed the common law "fiduciary exception" to the attorney-client privilege for communications between fiduciaries and trust lawyers on matters impacting trust beneficiaries and affects ultra-high-net-worth clients, their trust strategies and fiduciary administration through non-obvious ways vis-à-vis this passion asset class.

Consider the potential paralysis of a self-directed trust having an art collection. The fiduciary must warrant clear legal title for assets the trust loans for exhibition or sells. A fiduciary might seek legal advice about the ownership of the object at issue in the transaction, similar to in the real estate industry, a lawyer opinion letter (before the advent of real property title insurance).

Because the art title legal advice will be front and center if the trust suffers a title-related financial loss and when it is time to assign fault, the fiduciary may be reluctant to seek the opinion; and the trust's legal counsel will be reluctant to render an unequivocal or meaningful opinion. In the end, the fiduciary might face an E&O claim for failing by inaction to manage a key trust risk, and the UHNW client's trust directives will be unfulfilled. UHNW clients serving as museum trustees can find themselves in the same unwanted crossfire. ■

Lawrence M. Shindell is chairman of ARIS Title Insurance Corporation. ARIS is the recognized global authority on the subject of legal title risks impacting the global fine art and collectibles market. For more information, please go to www.aristitle.com and www.argolimited.com.