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Buyers Find Tax Break on Art: Let It Hang Awhile in Oregon

By GRAHAM BOWLEY and PATRICIA COHENAPRIL 12, 2014
Inside
Photo

Francis Bacon's "Three Studies of Lucian Freud," one of the most expensive works ever sold at auction, was lent to the Portland Art Museum.Credit Leah Nash for The New York Times

EUGENE, Ore. — The Jordan Schnitzer Museum of Art, tucked into a quiet corner of a college campus here in the hills of the Pacific Northwest, is hardly the epicenter of the art world. Yet major collectors, fresh from buying a Warhol or a Basquiat or another masterpiece in New York, routinely choose this small, elegant redbrick building at the University of Oregon to first exhibit their latest trophy.

The museum's intimacy and scholarship are likely to play some role in their choice. But a primary lure for the collectors is often something more prosaic: a tax break.

Collectors who buy art in one state but live in another can owe thousands, tens of thousands, even millions of dollars in state "use taxes": taxes often incurred when someone ships an out-of-state purchase home. But if they lend the recently purchased work first to museums like the Schnitzer, located in a handful of tax-friendly states, the transaction is often tax-free.

Beyond the benefit to museums, this lucrative, little-known tax maneuver has produced a startling pipeline of art moving across the United States as collectors cleverly — and legally — exploit the tax codes.

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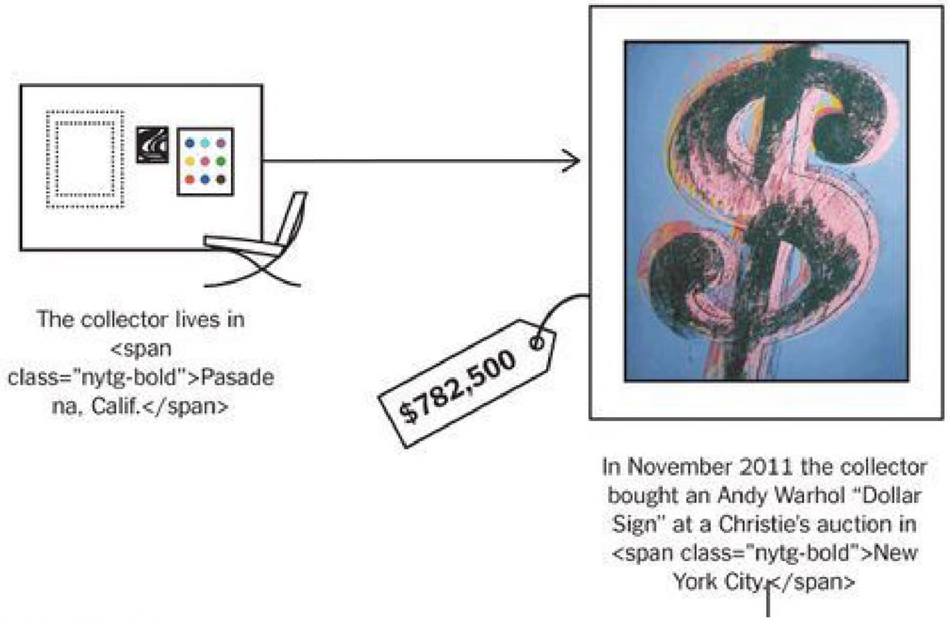
Graphic

How to Save $68,469 in Taxes

In some cases, collectors can avoid paying taxes on art they buy if they display it out of state before bringing it home. Here is how one collector navigated the system.



OPEN Graphic

Dozens of important works have come to the Schnitzer in recent years, largely because of the tax break, museum officials believe — so many that the museum has a program called "Masterworks on Loan"; the featured works are housed in a second-floor gallery.

Similar loans — which rarely extend beyond a few months — also flow into other museums in Oregon, and occasionally New Hampshire and Delaware, all states that have neither a sales nor a use tax.

The Portland Art Museum, for example, has a long history of receiving art loans from collectors, including, most recently, Francis Bacon's triptych "Three Studies of Lucian Freud," one of the most expensive paintings ever sold at auction.

Portland officials say collectors lend art for a variety of reasons, not just for the tax break. But only a few weeks after the painting sold for a stunning $142 million last fall at Christie's in New York, it landed, to the surprise of many, in the Portland museum, where it drew large crowds for 15 weeks.

By shipping the painting first to Oregon, instead of her home in Las Vegas, the new owner, Elaine Wynn, may be eligible to avoid as much as $11 million in Nevada use taxes, though it is not clear whether she intends to take advantage of the break.

Collectors typically learn of this strategy only through savvy lawyers, dealers and auction specialists. But within the circle of people who know of the practice, it generates debate between those who appreciate how it fosters public access to art and those who suggest that such access comes at too high a price to unwitting taxpayers.

For example, do taxpayers in, say, California even understand that they have given up millions of dollars in tax revenue over the years to, in effect, underwrite the display of paintings in other states?

"Some states are going to become aware of this and realize what potential revenue they are missing under the current laws," said Steven Thomas, a lawyer in Los Angeles who advises art collectors on tax matters.

Supporters defend the practice as an important way to ensure public access to significant art before it disappears into private collections. Robert Storr, the dean of the Yale School of Art, described it as a "great resource" for museums. At the Schnitzer, a teaching museum, curators and members of the faculty use the loans in their programs.

"The two museums, the Portland Art Museum and the Jordan Schnitzer Museum of Art, are the beneficiaries of getting amazing works of art that they would not get," said Jordan Schnitzer, a businessman and collector who donated millions of dollars to the Eugene museum that bears his name and served on the board of the Portland museum.

But critics of the practice also question whether museums curry favor with possible donors by accepting loans, and they complain that works are sometimes exhibited without the context or curatorial judgment that museums

traditionally provide. A recent visit to the Portland museum found some lent works exhibited haphazardly: a Cubist work from the 1950s, for example, placed amid American art from the 1980s.
"It is an amazing opportunity for these smaller cities to show these works," said Mack McFarland, a curator at the Pacific Northwest College of Art, in Portland. "But one does have to wonder, doing a cost-benefit analysis on a more global scale, whether or not the tax break for these wealthy collectors is worth it."
States employ use taxes to compensate for residents who avoid sales taxes by shopping in another state. The tax rate is generally the same as the sales tax, and people are supposed to calculate what they owe on items bought out of state, then pay that amount as part of their tax filings.
Art collectors who seek to avoid the tax typically offer a recently purchased work to a museum in one of five states — New Hampshire, Oregon, Alaska, Montana and Delaware — that do not have a use tax so that the loan does not incur a tax.
As long as the painting stays at the museum for an extended period, typically more than three months, before being shipped home, the practice in several states where collectors live, like California, is to regard the exhibition as a first "use" of the item and waive any tax. The result is a tax-free transaction.
The Hallie Ford Museum of Art at Willamette University in Salem, Ore.; the Delaware Art Museum in Wilmington; and the Hood Museum of Art at Dartmouth College in Hanover, N.H., are among other institutions where collectors have lent art because of tax considerations.
The tax strategy is 100 percent legal, experts say, as long as all stages of the museum transfer are handled correctly.
Schnitzer officials said that many California collectors had taken advantage of the tax provision. "We are on their way home," said Jill Hartz, the executive director of the museum.
California explicitly outlines a "first use" exemption in its tax code. It says that property, whether a couch or a Caravaggio, that is first "used" out of state for more than 90 days does not incur the tax.
Photo

Jill Hartz of the Jordan Schnitzer Museum of Art in Eugene, Ore., said art loans have aided its educational mission. (It is unclear if the owners of the works shown lent them for the tax considerations.)Credit Leah Nash for The New York Times
Experts said that for many years it was known in art circles as the "Norton Simon rule," because Mr. Simon, an industrialist who died in 1993, was one of the first art collectors to make ample use of it with loans to several museums like the Portland Art Museum.
States have no reliable calculus to measure what sort of tax revenue is being lost. But in a recent example, a California collector is eligible to save at least $390,000 by employing the tactic.

The collector bought a painting, “Ribs Ribs,” by Jean-Michel Basquiat, at auction in New York last year for $5.2 million. Since the painting was being shipped out of state, the new owner was not liable for the New York sales tax.
But the buyer would still have owed use taxes in California (which range from 7.5 percent to 10 percent of a sale price), had the work been sent directly there. Instead, the Basquiat went to the Schnitzer, a detour that meant that the collector was eligible for the first-use exemption, according to the dealer involved in the transaction.
“It is one thing if you are buying a pair of shoes or pots and pans,” said Anne-Marie Rhodes, a Loyola University Chicago law professor, “but in these times, when regular taxpayers have it so difficult, to have such an easy way to avoid the use tax is hard to justify.”
Collectors who live in states that don’t recognize a first-use exemption are out of luck. New York, for example, typically imposes a use tax — 8.875 percent in Manhattan — on art brought into the state by a resident, even if it is first publicly displayed elsewhere.
Collectors, of course, routinely lend to museums for reasons that have nothing to do with a tax break. They want to educate the public, perhaps, or seek advice on conserving a work.
Andrew Teufel, a San Francisco private investor and collector who has lent many works without any tax consideration, said he lent one work, a Kay Sage painting now at the Schnitzer, that will qualify for the tax break. But he said he primarily lends art to enrich others, as well as to bolster its provenance and value.
“The tax preference is the icing on the cake,” he said.
Jerry Kohl, a California businessman, took the tax break when he lent a Warhol to the Schnitzer two years ago. But he said he would have made the loan even without any tax consideration. Still, he said, he thinks the tax code should be tightened.
“The provision should require owners to lend a work out at least every five years instead of just once,” he said.
In Portland, the use of the tax break took off in the 1990s, when the museum’s executive director was John E. Buchanan Jr., according to his widow, Lucy Buchanan. She said he built relationships with West Coast collectors whose loans helped the museum raise its profile.
In those years, questions arose about the sudden arrivals of unannounced loans, which were disruptive to the museum, said Kristy Edmunds, a former curator there who is now the executive and artistic director of the Center for the Art of Performance at the University of California, Los Angeles.
“Crates would land on the loading deck,” she said, “and everyone would be calling up, ‘What is in this shipment?’ ”
Current Portland museum officials said they did not promote the tax break. But they acknowledged that they had had to initiate a policy to deal with unsolicited offers for short-term loans that says that they must be approved by the director, and others, to ensure that the art meets the museum’s standards.
Ms. Wynn, the ex-wife of the casino magnate Steve Wynn, declined to respond to requests to detail her tax plans for the Bacon triptych, which was on display in Portland until last week. Museum officials said that they knew nothing about them.
They said the triptych came to the museum because the museum’s chief curator, Bruce Guenther, reached out to the owner shortly after the sale. (Museum officials have not identified the owner of the triptych, but art world sources have named Ms. Wynn.)
The museum said that tax considerations were not part of the discussions and that the owner had been impressed by the museum’s commitment to display the work prominently.
Brian Ferriso, the Portland Art Museum’s director, said his institution insisted in most cases that a work of art be lent for at least 120 days, not 90, to give it greater public exposure but also to avoid any appearance that its program exists purely to fit the prerequisites of the California tax provision.
“We want to be seen as an institution that is putting art on the wall in a transparent fashion,” he said.
Robin Pogrebin and Carol Vogel contributed reporting from New York.

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