



ILLINOIS STATE BAR ASSOCIATION

TRUSTS & ESTATES

The newsletter of the Illinois State Bar Association's Section on Trusts & Estates

The fine art of fine art investments

By Jesse T. Coyle, J.D., LL.M.

In recent years, fine art has increasingly been viewed as a wise alternative investment and as a means to better achieve diversification. The low correlation of fine art to more traditional markets and a reasonable risk to reward ratio makes it an attractive investment for some. But amateur investors should proceed with caution because the illiquidity of art and the irrationality in the art market makes it difficult to benchmark against more conventional investments.

The Numerous Benefits of Investments in Fine Art

Fine art as an investment can be very attractive for several different reasons. First, fine art tends to have a low, and occasionally inverse correlation with many traditional investments, such as equities. Therefore, placing fine art in your portfolio can mean better diversification and can possibly hedge against some stock market fluctuations. Second, for those that find fine art appealing, investing in fine art is not merely a financial investment, but also a personal investment. Unlike shares of stock that cannot be enjoyed separate from their financial characteristics, artwork provides often unmatched aesthetic pleasure. So not only is it an investment that can increase your net worth over time, it is also a way to add beauty to your home and increase the artistic appreciation within your family. Third, as the popularity of investing in art has increased, so has the availability of art related investments and art advisors. Notably there are fine art investment opportunities apart from simply purchasing an individual painting or sculpture for your home such as investing in various art indexed funds. And when considering whether to purchase a piece of art, there are

a multitude of advisors that can assist you in this endeavor. Most of these advisors provide fee-based services.

The Mei/Moses Fine Art Index can be utilized to assess the value of the fine art market. The Mei/Moses Fine Art Index tracks thousands of pieces of art that have been auctioned since 1950 and measures the value of the art market by analyzing repeat sales of the different pieces of art that are located in the index. But while it is considered a fair benchmark for art valuation it still has some notable deficiencies as it excludes transaction fees, works that fail to sell at auction, certain styles of art (such as photography and prints), shipping costs, and insurance fees, all of which can affect the actual cost and value of a piece of art.

For the investor that wants to find a way to invest but also wants to engage in an enjoyable and invigorating hobby, investing in fine art may be the perfect fit. As a rule of thumb, art collecting is best accomplished by someone who appreciates and enjoys art, not just an individual who is simply trying to make a quick profit. But if collecting art is new to you, and unless you have the time and experience to master art investments, it may be wise to seek the assistance of a professional before jumping headfirst into any large fine art investment.

Art is a more flexible asset than many people realize. For example, instead of simply allowing art to remain in an individual's estate upon his or her death and then have it sold by the individual's children for less than what it is worth, art can be given to charity, sold to a museum, kept in a trust, or gifted to heirs, amongst other alternatives.

The art market is extremely diverse and global (and becoming increasingly so with

the rise in global high net worth individuals), thereby allowing individuals to invest in anything from medieval German paintings and sculptures to prints and paintings from upcoming artists from the Chelsea neighborhood of Manhattan. Many Western collectors are even favoring art from emerging markets such as Russia, India, China, Poland, and Cuba. These markets generally do not have the same export restrictions and regulations which some Westernized countries place on historical pieces.

Notable Concerns Regarding Investments in Fine Art

Even though the benefits of investing in fine art are numerous, there are also several concerns of which a would-be investor needs to be cognizant.

One serious concern is that art is not a liquid asset for which there is an easily accessible market. Non-marketable assets like fine art have serious intrinsic risks as both value and demand can be hard to calculate. For example, Modern and Impressionist art were once the most popular fine art categories and brought in the highest value upon sale; in contrast, there are now indications that Contemporary art has surpassed both Modern and Impressionist art in popularity. These social caprices exist entirely separate from any rhyme or reason, but nevertheless can thoroughly affect the value of fine art.

The art market is generally less predictable than the financial markets and therefore it is often difficult to determine what would be a reasonable expectation for return on a particular art investment. In the Estate of Georgia O'Keeffe, the court stated: "A work of art usually does not have intrinsic financial value beyond its desirability as art and lacks

external indicia of return prior to sale, such as earnings or investment.” Additionally, art market indexes (i.e. The Mei/Moses Fine Art Index discussed above) do not truly encapsulate the art market as many works of art are sold privately and away from public auctions.

Many people simply cannot financially afford to enter into the art market as serious investors. Those that can afford to enter into the market may still be surprised by the

cost of the endeavor as many of the art funds available to investors can be burdensomely expensive. To boot, the pieces of art that tend to offer the greatest security from downward fluctuation are often the most expensive. Additionally, the purchase of art can come with sizeable expenses through auction fees (which can occasionally be as high as 30 percent), insurance costs, and expensive shipping costs.

Conclusion

Investing in art can be an exciting opportunity for many individuals to make great profit, diversify a portfolio, and to add aesthetic beauty to an individual's home. But as with all investments, engaging in the collection of art for investment purposes carries its own unique risks that should thoroughly investigated and evaluated. ■

THIS ARTICLE ORIGINALLY APPEARED IN
THE ILLINOIS STATE BAR ASSOCIATION'S
TRUSTS & ESTATES NEWSLETTER, VOL. 55 #6, APRIL 2009.
IT IS REPRINTED HERE BY, AND UNDER THE AUTHORITY OF, THE ISBA.
UNAUTHORIZED USE OR REPRODUCTION OF THIS REPRINT OR
THE ISBA TRADEMARK IS PROHIBITED.