THE ART OF NEW YORK LIVING

Art for Pension Portfolios?

By Kenneth Jay Linsner

Suggested changes in the Social Security System have raised some eyebrows across the spectrum of professional investors. What then of what the UK plans to do? European financial observers are predicting that changes to that country's pension laws next year will allow for the inclusion of art in pension portfolios.

If all goes according to schedule, from April 6, 2006 those individuals with a 'self invested' pension plan…the road on which we may be starting, will be permitted to purchase a wider variety of assets including paintings antiques and wines. Larger pension funds, such as the two proposed in this country, will also be able to take advantage of this, but it seems most likely that individuals who establish their own portfolios will be the ones to exercise the change.

Those who already own works of art will be able to transfer them to their own portfolios. The downside to this, at least in the UK, is that such a transfer will be considered 'a sale' and will generate capital gains taxes from amounts over about $10,000. Of course, if the artwork has not appreciated in value since the date of acquisition it would not trip any tax burden. While not yet defined, it seems that the fair market value of the artwork (the price most likely to be brought by auction sale of the property) would be the determining factor. If bought at the retail level of trade, the original purchase price would have to adjusted to the fair market value level as of the date of purchase in order to determine the amount of capital gains, if any, to be paid upon transfer. The other wrinkle in this scheme is that if the self-generated portfolio decides to keep the artwork (or wines) in the residence of the investor, then there will be a yearly 'tax' to be paid. This 'tax' is not imposed on loaned or stored works of art, wines or antiques. The good news is that any artwork, antiques or wines (one assumes they also mean to include decorative arts of any period) left in portfolio upon the demise of the investor will be free of estate taxes. The UK rules will, however, force all individuals to sell such non-income producing assets by age 75.

There are, however, some points in the above, which have troubled the UK's Inland Revenue Service (IRS). As an example, what would happen if a painting worth $500,000 were in the pension fund of a father with a majority interest of, say, $400,000, the fractional balance being claimed as an interest by his daughter in her pension fund. It would have to be sold when the father reached the age of 75, but the daughter's minority interest in the work would limit the amount for which the painting could be sold. While this could reduce the price to a point where no capital gains tax was owed by the father, if the daughter where the buyer, it would allow for a transfer of ownership to the next generation prior to the demise of the original investor while keeping the sale proceeds within the family. The UK proposes to cap the amount of artwork allowed in a personal portfolio at about $2,000,000.

Having been advisor to an art investment fund in the Netherlands and with the news that Artemis Fine Arts, the long-time art investment group in London, has suffered another loss and has appointed a team of specialists to find a buyer I pause when reflecting on the above. The problems that individuals would face with assessing condition, true fair market value and venues for the acquisition or re-sale of any non-incoming producing asset (read artwork), should make those investors pause as well. I have said before and will state again here, that art is not an investment in the true sense of the word. Only specialists who can buy 'surgically' taking chances across a whole spectrum of items that are bought for a perceived 10-20% of what the re-sale value might be can hope to succeed in this…and "this" is a full time job … another part of New York Living.