

CHUBB COLLECTORS



Who Owns Your Art?:

The Importance of Due Diligence for Fine Art Collectors

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Background

While a popular crime from time immemorial, art theft truly exploded during World War II. The Nazis stole or forcibly sold off at least 20% of all art in Europe. This involved a staggering five million art objects. Following the war the Allies made a concentrated effort to locate and return these displaced works, but this noble effort fell far short, leaving an enormous trove in government “storage” or in museum collections. Other works found their way back into the Western European and North American art markets via shadowy networks of dealers and galleries, while a lax and sometimes complicit art market eagerly pedaled them to largely naive museums and collectors.

Robert M. Edsel, author of *Rescuing Da Vinci* (Laurel Publishing, LLC 2006), explained that several elements have helped these problems surface after decades underground. First, the Internet has allowed for the zero-cost dissemination of photographs amongst collectors, auction houses, museums, and academics. Secondly, the opening of archives and museums in the former Soviet Bloc has allowed unprecedented access to records, and thirdly, art as an asset class has gained wildly in terms of popularity amongst investors – not collectors or art aficionados, necessarily – but investors. Everyone is in the game now. Finally, with the generational transfer of assets to the Baby Boomers, works of art are now coming into the hands of family beneficiaries and estate lawyers.

Art theft did not begin with the Nazis nor did it end with them. To this day, art remains a favorite target of criminals for the same reasons it always has: availability, portability, demand, and profit.

How Do Private Collectors Obtain Stolen Art?

Art changes hands in many ways. These include private sales; sales by dealers; sales at auction; transfers by donation or bequest; and of course, direct sales by the artist, yet there are, generally speaking, no federal, state, or local governing bodies or agencies tasked with regulating art sales. Some states have enacted certain laws special to art sales, while overall, sales of art are governed by the Uniform Commercial Code (UCC), as enacted in the various states.

For concerned collectors the aspect of commercial law most noteworthy is that pertaining to title. Before the UCC was enacted, the familiar doctrine of caveat emptor prevailed, allocating risk of bad title to the buyer. Under the UCC however, this risk has been shifted back to the seller. The UCC provides that, unless specifically excluded or modified, every sale contract includes an assertion that title to the work is good; that the seller has the right to transfer title; and, that the work is delivered free from any lien or encumbrance.

So, if art sales are typically accompanied by a warranty of good title, why is stolen art cause for concern? The answer is simple; a warranty of good title applies at the back end of the transaction. At the front end, works of art make their way into the marketplace from innumerable sources, and could have changed hands many times before winding up in an auction catalogue or gallery window. Moreover, the back-story is most often

obscured by a time-honored cloak of confidentiality. Therefore, when an Old Master painting appears on the market, there remains, not infrequently, a substantial veil of mystery surrounding the work. Consider, then the level of assurance afforded by a warranty of title: it tells you that you have a remedy, but not whether you will need it.

When The Rights Of A Theft Victim And An Innocent Purchaser Collide

A bedrock principal of American commercial law is that a theft spoils title, and as a result one cannot obtain good title from a thief. This means that an innocent or “bona fide purchaser of stolen goods has no claim to title (i.e., his title is void), and therefore he has no defense to a timely claim brought by the actual owner or theft victim. The same would be true for a second or third generation bona fide purchaser, and so on.

All states have statutes of limitation – commonly four or fewer years, and most often two years. Once expired, the claim is thereafter time-barred. But, there is an exception to this rule: the statute of limitations governs the time within which a claim must be brought unless, in the exercise of reasonable care, the victim neither knew nor could have known that there was a claim to be made. For example, medical malpractice allows for the filing of a lawsuit many years after surgery during which an instrument was left behind. Until symptoms flare up, the patient would have no way of knowing within two years of the surgery that he had been the victim of medical malpractice.

In the case of art theft, unless or until the victim finds his stolen property, he knows not whom to sue. Hence, ownership rights can remain unstable for decades after a theft. Ultimately, when the theft victim and latter - day owner collide, the victim’s lawsuit is deemed timely so long as it is filed within the period of the “discovery date” plus the original limitations period.

Title Due Diligence Can Immunize A Subsequent Purchaser

Courts have counseled collectors to investigate artworks before buying them. As the United States Court of Appeals for the Seventh Circuit instructed: “[T]hose who wish to purchase artwork on the international market, undoubtedly a ticklish business, are not without means to protect themselves. Especially when circumstances are suspicious, prospective, purchasers would do best to do more than make a few last-minute phone calls.”

To encourage such investigation courts “balance the equities ” between the parties. As one commentator explained, “courts will measure the steps the person in inadvertent possession of stolen art took to avoid acquiring it, against the steps the former owner took to report the loss and make it known to the art world.”

For a variety of reasons courts view this equitable scale as tilted initially in favor of former owners. Moreover, courts have recognized that art theft victims face many difficulties in finding their stolen art in an international market that prizes privacy and secrecy. In addition, “under this balancing test, greater diligence will be required of wealthy collectors with special resources and sophistication, or when the work in question is valuable.” So unless collectors and their advisors can show that they took informed precautions, former owners will prevail in this balancing test.

Due Diligence Methods and Resources

No court has prescribed specific steps that satisfy due diligence responsibilities. Nonetheless, both courts and commentators have identified stolen art databases, organizations and other art world contacts and resources that collectors and their advisors can consult to discharge their investigative duties. These include inquiries to:

- internet stolen art databases (see previous articles *The Art Loss Register*, Kisluk, 2001; *Lost and Found*; *The Use of International Art Registries For Identifying and Tracking Valuables*, Staff Writer, 2008.)
- experts in the particular artist or type of work;
- the applicable catalogue raisonné of the artist (if available);

- museums with prominent collections of the works of the artist;
- international auction houses;
- dealers and galleries that specialize in the artist or type of work;
- collectors groups and specialty publications;
- cultural organizations and other NGOs specializing in fine arts and cultural property;
- governmental sources such as the country of origin of the work;
- law enforcement; and,
- professional due diligence / title research firms.

For collectors who lack the time or know-how to conduct self-directed title research, there is also the option of a due diligence investigation, also known as title due diligence, by an experienced researcher. Hiring a title research firm or attorney can provide the most comprehensive solution to the risk of defective title.

One such title due diligence firm is Art Title Advisors, LLC. (ATA, www.arttitleadvisors.com). With its services available exclusively to Chubb Valuable Articles Coverage (VAC) policy holders, for a fee ATA performs title research and produces an Ownership Rights Protection Report which indicates whether title to a work is defective or clouded. In the event of a title dispute, a collector holding an ATA report will be able to demonstrate that he or she took reasonable steps to determine whether there was a problem with title. This is a most advantageous position, in that courts will typically consider the collector's ownership rights against the backdrop of due diligence. That is to say, collectors who cannot demonstrate due diligence will be hard-pressed to defend their claim to works later shown to suffer from a defect in title.

In several states Chubb affords an enhancement to its VAC coverage, providing up to \$100,000 towards legal fees associated with a title dispute in which a policyholder is defending his title. According to Worldwide Fine Art Manager Dorit Straus, Chubb has come up with, "an innovative solution to a very difficult problem. The two-pronged approach provides universal defense costs to all customers with fine art, as well as an exclusive service to research provenance and get a report that will protect them in future claims." Together with the Ownership Rights ProtectionSM Report this coverage enhancement, which is available at no additional charge, comprises what Chubb refers to as its Art Title Solution.

A different approach is title insurance, currently available through a very small number of carriers. This is based on a traditional indemnity model and provides coverage in the event that a title dispute results in the loss of ownership.

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