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THEY CAN'T TAKE MY PAINTING, CAN THEY? : PROTECTING YOUR ARTWORK FROM GALLERY CREDITORS

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As the art market is coming to grips with the adverse effects that the Coronavirus is having on art galleries around the world, collectors in the United States should immediately reevaluate any artworks on consignment or loan with galleries to insure that they can recover their art in the event of the insolvency or bankruptcy of such galleries.¹

With many galleries under financial strain from the diminished sales resulting from today's health crisis, it is likely that over the coming weeks and months we will see many galleries succumbing to the debt and expense burdens inherent to their businesses. In such cases, a gallery's secured creditors, especially those with either all asset liens or liens in the gallery's current or hereafter acquired inventory, will enforce their rights to foreclose on the gallery's assets, which to the surprise of many an art collector might include his or her artworks.

If a collector in the U.S. has consigned a work of art for sale with an art gallery, the collector runs the risk of losing the artwork to competing claims of secured creditors of the gallery if said collector did not properly perfect his consignment agreement according to the applicable state's Uniform Commercial Code ("UCC").²

Under the UCC, a collector must take the following steps to protect his consigned art against the interests of the gallery's secured lenders or other creditor with a prior blank security interest in the gallery's inventory:

- The collector must have entered into a proper consignment agreement with the gallery, which should ideally (i) clearly identify the artwork being consigned, (ii) confirm that title in the work does not pass until full payment has been received by the collector, (iii) acknowledge the rights of the collector as a secured party under the UCC with respect to the artwork and any sale proceeds, (iv) require the gallery to defend the collector's rights against any such creditor, (v) identify the artwork as consigned property and not designate the artwork as the gallery's inventory, and (vi) authorize the collector to file such UCC financing statements and to provide such notices to the gallery's creditors as necessary to perfect the collector's security interests.

¹ Galleries that have consigned or loaned artworks to other galleries from either its own inventory or from its collectors should also review their consignment and lending arrangements with such other galleries.

² It is worth noting that most states in the U.S., including New York, provide special protections for artists with respect to their consigned artworks and proceeds from the sales of their artworks. Such protections generally trump the claims of a gallery's creditors with respect to any such artist-owned artworks and earned but unpaid sales proceeds.

- The collector must file a UCC-1 Financing Statement with the State of the gallery's formation or incorporation, as the case may be, naming the consigned artwork with specificity³, properly identifying the gallery by legal name and address, and confirming the existence of the consignment by checking the consignor/consignee box on the form.
- Prior to the gallery's receipt of the consigned artwork and no more than 5 years before such receipt, the collector will have sent an authenticated notification to the Gallery's creditors holding conflicting security interests in the gallery's inventory describing the artwork with reasonable specificity and stating that the collector is the owner of the artwork, the collector intends to consign the artwork to the gallery for sale, the artwork is not inventory of the gallery and the collector has a consignment interest in the artwork.

Owing to the many steps and costs involved in properly perfecting a security interest as well as past experiences without adverse outcomes, many collectors elect to forgo one or more of the aforesaid requirements and in doing so, fall victim to their own hubris and nonchalant attitudes toward art consignments, eventually losing their artworks to judicial liens and perfected security interests of bankruptcy trustees, the gallery's lenders or other debtors-in-possession of the artwork.

If a collector finds themselves in such an unperfected position, it is imperative that they take immediate steps to:

- identify their consignments by filing UCC-1 financing statements against the gallery;
- demand that the gallery adequately document their consignment if done on a handshake or other informal means;
- require the gallery to disclose the location of the collector's artworks; and
- if possible and permissible under law, retake possession of the art from the gallery until the consignment agreement can be properly perfected.

It is worth noting that collectors need not only evaluate their consignments for sale but also their exhibition or artwork loan agreements with a gallery. If a collector provides an artwork for an upcoming retrospective or other non-selling exhibition at a gallery, the collector must be sure to avoid certain pitfalls that could cause what is essentially a bailment of the artwork to unintentionally become an unperfected consignment of such work subject to the gallery's creditors.

Some basic rules of thumb that a collector can be guided by are as follows:

³ Artwork descriptions should include the artist's name, title of the piece, date of creation, medium, dimensions, edition number and size if not a unique work and other identifying information.

- Include a provision in the loan agreement that prohibits both the sale or offer of sale of the loaned art work;
- Require that proper credit be given to the owner of the loaned work⁴ at the point of display of the artwork and in any printed or online catalogue of the exhibition;
- Affix an address label to the back of the frame of the artwork identifying the name and address of the owner;
- file a UCC-1 Financing Statement with the State of the gallery's formation or incorporation, as the case may be, naming the loaned artwork with specificity, properly identifying the gallery by legal name and address, and confirming the existence of the loan by checking the bailor/bailee box on the form;
- Demand that the gallery adequately document the artwork loan and not rely on a handshake or other informal means; and
- If the loaned artwork is to be insured by the gallery, name the collector as an additional insured and loss payee on the gallery's insurance.

While it is imperative that everyone provide support at this critical time for the many galleries that represent the art market's very foundation, it is also important for market participants to make sure that their consignments and loans are properly documented to protect their valued artworks.

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⁴ It is okay to specify that the work is on loan from a "private collection" as opposed to specifying the actual name of the owner.