Pioneer Bank & Trust
Trust & Investments
Local.

704 7th Ave, PO Box 729
Belle Fourche, SD 57717-0729
Phone (605) 892-3494
Fax (605) 892-2115

2001 W Omaha St, PO Box 9189
Rapid City, SD 57709-9189
Phone (605) 341-2265
Fax (605) 341-7425

140 E Jackson Blvd, PO Box 10
Spearfish, SD 57783-0010
Phone (605) 642-2725
Fax (605) 642-1736

The tax value of fine art

Bernice Newberger died in July 2009. Her estate included three valuable pieces of art, for which it obtained appraisals from Sotheby's and Christie's. The valuation was complicated by the fact that the market for fine art took a steep dive in 2008, as the economy slipped into recession. For example, in October 2008 some 44% of pieces put up for auction failed to attract minimum bids, double the rate of a year earlier. They had to be returned to their owners. In 2009 Sotheby's revenue declined by 53% and Christie's by 46%. Bernice's death came at the trough of the slump.

Based upon the advice of appraisers, the estate valued two lesser pieces at $450,000 and $500,000. The real prize was a Picasso. Sotheby's offered a $3.5 million guaranteed price. Christie's offered the estate better guarantees and a professional estimate of date-of-death value of $5 million, which the estate duly included on its estate tax return, timely filed in October 2010.

The IRS challenged all three valuations. Perhaps to create some liquidity for paying taxes, the estate had accepted the terms from Christie's and put the Picasso up for auction in February 2010. The expected sale price was $4.7 million to $6.3 million, consistent with the appraisal. In the event, including the buyer's premium, the painting fetched over $12 million. The IRS cited that fact as it claimed that the Picasso had been undervalued by the estate.

Although events occurring after death are not to be taken into account to determine date-of-death values, the Tax Court held that the later sale may be used as *evidence* of value. The estate's argument that the high price was "a fluke" that was unforeseeable at the date of death was rejected. The Court accepted the IRS' downward adjustment to $10 million to reflect the changing market conditions. The estate's values for the two lesser pieces were sustained.

Had Newberger lived another seven months, her estate would have avoided all estate taxes, as 2010 was the year when the federal estate tax was optional. In the absence of estate tax, carryover basis would apply. In that event the heirs would have been exposed to a very large capital gains tax upon the sale of the art, as Newberger had acquired the Picasso for just $195,000 in 1981.

(February 2016)