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Robson, Deirdre ORCID logoORCID: <https://orcid.org/0000-0002-6763-0352> (2019) A law of "unintended" consequences? United States federal taxation and the market for modern art in the United States. *Journal of Art Market Studies*, 3 (1). pp. 1-16.

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A Law of “Unintended” Consequences? United States Federal Taxation and the Market for Modern Art in the United States

ABSTRACT

This article aims to explore a to-date little considered nexus between U.S. Federal taxation and the American art market. Lacking so far in an increasing body of studies of the relationship between tax policy and the arts is a discussion of impacts which Federal taxation might have had upon the American art market for modern art rather than arts sector more generally. The scope of this article is two-fold: first, to posit a nexus between Federal revenue

codes and the systemic structure of the nascent New York market in the mid-twentieth century; second, to explore how the radical tax reforms of the 1980s impacted on the New York art market and collector preferences. In relation to this, this article will explore two cornerstones underpinning Federal taxation: first, the tax-exempt status given to non-profit institutions; second, the charitable deduction allowed against Federal tax (personal income tax, estate tax) liabilities as part of the American ethos of indirect giving.

This article aims to explore a to-date little considered nexus between U.S. Federal taxation and the American art market. The intention is to add to the literature discussing Federal government and the arts: for instance, the relationship between Federal tax policies, tax reforms, and tax giving; or Federal tax and art museums.¹ Although gov-

1 Including: J.Mark Davidson Schuster, The Interrelationships Between Public and Private Funding of the Arts in the United States, in *The Journal of Arts, Management and Law*, 14/4 (Winter 1985), 77-105; Gerald E. Auten, Charles T. Clotfelter, and Richard L. Schmalbeck, Taxes and Philanthropy Among the Wealthy, in Joel Slemrod, ed., *Does Atlas Shrug? The Economic Consequences of Taxing the Rich* (New York: Harvard University Press, 1997); Charles T. Clotfelter & Thomas Ehrlich, eds., *Philanthropy and the Nonprofit Sector*

ernment support for the arts has been a commonplace in Europe, opinion in the United States has been quite hostile to the idea. The arguments against public financing for the arts in the United States include the view that direct Federal support for the arts was too costly; the arts, as a private or local concern, were not a proper concern for Federal government; Federal support would result in federal interference and control.² While in 2000 Finland spent \$111.67 per citizen, with Germany second at \$89.52 per person, the United States ranked last, with Federal support a miserly \$5.85 per capita.³ Despite appearances, however, the United States has been a leader in private support funded by tax breaks. Indeed, the importance of this, a form of “indirect funding,” has been such that Feld et al describe it as being “like an underground river” which “affects the arts profoundly,” and which by 1983 amounted to two-thirds of all the support received by American arts organisations.⁴ What is lacking so far in an increasing body of studies of the relationship between tax policy and the arts is a discussion of impacts which Federal taxation might have had upon the American art *market* for modern art rather than arts sector more generally. The scope of this article is two-fold: first, to posit a nexus between Federal revenue codes and the systemic structure of the nascent New York market in the mid-twentieth century; second, to explore how the radical tax reforms of the 1980s impacted on the New York art market.

With the Sixteenth Amendment (1913) the United States government for the first time moved from raising revenues solely via excise duties to a system of income tax and commitment to taxing people according to their ability to pay. Alongside this a central tenet was that Federal government should be unobtrusive, not the primary source of public expenditures (except in areas such as military spending), and committed to incentivising individual philanthropy and support for non-profit organisations or institutions. Such “indirect” support is based on the concept of tax expenditures: losses in revenue are allowed “to promote some societal good without the government directly incurring the cost.”⁵ In this, two “cornerstones” underpin Federal policy: first, the tax-exempt status given to non-profit institutions; second, that deductions for contributions were allowed

in a *Changing America* (Bloomington: Indiana University Press, 1999); Jon Bakija, Tax Policy and Philanthropy: A Primer on the Empirical Evidence for the United States and Its Implications, in *Social Research*, 80/2 (Summer 2013), 557-582; Leila John, Museums and the Tax Collector: The Tax Treatment of Museums At The Federal, State and Local Level, in *Univ. of Pennsylvania Journal of Business Law*, 15/3 (2013), 878-920.

2 Gary O. Larson, *The Reluctant Patron: The United States Government and the Arts, 1943-1965* (Univ. of Pennsylvania Press, 1983), 7. See also: Alan L. Feld, J. Mark Davidson Schuster, and Michael O'Hare, *Patrons Despite Themselves: Taxpayers and Arts Policy (A Twentieth Century Fund Report)* (New York: New York University Press, 1983); James Heilbrun and Charles M. Gray, *Economics and Arts and Culture* (London: Cambridge University Press, 2001).

3 Heilbrun and Gray, *Economics and Arts and Culture*, 139.

4 Feld et al, *Patrons Despite Themselves*, 2.

5 Vada Waters Lindsey, The Charitable Contribution Deduction: A Historical Review and a Look into the Future, in *Nebraska Law Review*, 81 (2003), 1056-1096, 1057. See also: J. Mark Davidson Schuster, Issues in Supporting the Arts through Tax Incentives, in *The Journal of Arts Management and Law*, 16/4 (Winter 1997), 31-49.

against Federal tax (personal income tax, corporation tax, estate tax) liabilities.⁶ Under the former tax-exempt status is given to all institutions and organisations “organized and operated exclusively for religious, charitable, scientific, literary, or educational purposes” as set out in the 1917 Revenue Act.⁷ After this date, art museums were typically chartered as “charitable” and/or “educational” institutions to have tax-exempt status, and this has remained the same. The second “cornerstone” is particularly important for this article. There were changes in operation over the years, but the underlying principle remained unchanged. From 1917 onwards, Section 170 (c) of the Revenue Code allowed that “a contribution or gift to or for the use of ... a corporation, trust, or community chest, fund or foundation organized and operated exclusively for religious, charitable, scientific, literary, or educational purposes (including the encouragement of art and the prevention of cruelty to children or animals)” could be deducted from an individual’s tax liabilities (whether income or estate): the so-called “charitable deduction.”⁸ The original intention was to encourage continued philanthropic giving by insulating this from high income tax rates (raised significantly in 1917 to finance the war effort). Benefits for the individual of Section 170 relate to the Federal tax system, which, from 1913 onwards was a “layer cake” of up to twelve bands, each taxed at a different rate. Among taxpayers who itemized their deductions from tax (the wealthy), each additional dollar donated reduced income tax liabilities by one-dollar times the taxpayer’s marginal (top) tax rate.⁹ This was important because it impacted upon the so-called “price” of giving. For a hypothetical taxpayer in the highest income group, with a top marginal rate of seventy-eight percent, the “price” of giving would be twenty-two cents in the dollar; if the top tax rate was thirty-five percent it would be sixty-five cents.¹⁰ As will be seen, this had varying impacts at different periods. Moreover, if the original aim of Revenue Code Section 170 was to ensure the continuance of existing patterns of private philanthropy by the wealthiest the charitable deduction was soon seen as the “logical consequence of private giving to a public cause.”¹¹ How the “charitable deduction” was calculated is also particularly significant for this discussion. For gifts of money, the value of any charitable donation was calculated at cost (the amount given). However, for appreciated assets (such as artworks)

6 Charles T. Clotfelter, *Federal Tax Policy and Charitable Giving* (Chicago: University of Chicago Press, 1985), 11.

7 Don Fullerton, Tax Policy Toward Art Museums, in Martin Feldstein, ed., *The Economics of Art Museums* (National Bureau of Economic Research Conference Report), (Chicago: University of Chicago Press, 1991), 204-6; Randolph E. Paul, *Taxation in the United States* (Boston: Little, Brown & Co., 1954), 420-421.

8 Section 170 (c), ‘Charitable Etc. Contributions and Gifts’, IRC Tax Code, 1954. See also: Lindsey, The Charitable Contribution Deduction: A Historical Review and a Look into the Future, 1056-1096; Anne-Marie Rhodes, Big Picture, Fine Print: The Intersection of Art and Tax, in *Columbia Journal of Law and the Arts*, 26/2 (2003), 179-199; J. David Tracy, Charitable Gifts of Appreciated Property, in *SMU Law Review*, 25 (1971), 710-744.

9 Bakija, Tax Policy and Philanthropy, 557. See also: Clotfelter, *Federal Tax Policy and Charitable Giving*; Heilbrun and Gray, *Economics and Arts and Culture*; Paul, *Taxation in the United States*.

10 Clotfelter, Charitable Giving and Tax Policy in the U.S., CEPR Draft 050712, 2012. Available at www.parisschoolofeconomics.eu/IMG/pdf/may2012-paris-clotfelter.pdf, 7.

11 Feld et al, *Patrons Despite Themselves*, 196.

the value of donations was for many years calculated at “fair market value” (“the price at which the property would change hands between a willing buyer and a willing seller ... both having a reasonable knowledge of relevant facts”)¹² rather than “base” (original) cost. Moreover, opportunities for reducing tax liabilities via the “charitable deduction” were not solely linked to income tax: Revenue Code Section 2055 allowed the value of charitable bequests (calculated at “fair market value”) to be deducted from the gross value of any estate.

In examining the potential impact of Federal taxation upon the New York art market for modern art, the first focus of this article is the period of the 1930s through to the 1960s. This is for two reasons: first, not only was the Federal Revenue landscape set up – introduction of income taxes for the very wealthy (1913), estate tax (Revenue Act 1916), and the “charitable deduction” (Revenue Act 1917) – but this time was also characterised by an ongoing consensus that progressive taxation was “one of the central ideas of modern democratic capitalism”;¹³ second, this was the period during which the New York market for modern art developed its characteristic systemic structure. In this period, in line with the ongoing commitment to the ethos of progressive taxation, marginal income tax rates were high. During the 1930s, top rates were raised successively, and by 1939 stood at seventy-nine percent on incomes of \$1 million and over. In 1948 the top marginal rate on incomes of \$200,000 or more was eighty-two percent; in the 1950s it was up to ninety-one percent for incomes of \$300,000 or more. From the 1960s through the 1970s the top marginal rate was never less than seventy-seven percent.¹⁴ Paradoxically, high marginal rates of tax made philanthropy attractive to the very wealthy. For instance, if a hypothetical individual in the 1950s had a taxable income of \$65,000, they would be liable to pay fifty-seven percent on the first \$60,000 and seventy-eight percent on the excess above \$60,000. The same hypothetical individual, if having a taxable income in the next tax bracket down (\$50,000 to \$60,000), would be expected to pay fifty-three percent on the first \$50,000 and seventy-five percent on the excess over \$50,000.¹⁵ In the late 1950s, when the theoretical marginal rate was ninety-one percent (incomes of \$300,000 plus), only fifty-two percent of this was typically collected because of allowable deductions.¹⁶ As noted above, paradoxically high marginal tax rates made gifting more attractive: in 1960, with a ninety-one percent marginal tax rate the “price” for the wealthiest of making a cash donation was only nine cents per \$1 gifted. The situation was similar with respect to Estate taxes. As rates were highly progressive (up to sixty percent in the late

12 Treasury Reg. #1.170-1 (c)(1) 1988. See also: Konrad J. Liegel, Impact of the Tax Reform Act of 1986 on Lifetime Transfers of Appreciated Property for Conservation Purposes, in *Cornell Law Review*, Vol. 74/4 (4 May 1989), 745.

13 Walter J. Blum and Harry Kalven, Jr., The Uneasy Case for Progressive Taxation, in *The University of Chicago Law Review*, 19/3 (Spring 1952), 1952, 417.

14 Clotfelter, Federal Tax Policy and Charitable Giving, 31; Thomas L. Hungerford, Taxes and the Economy: An Economic Analysis of the Top Tax Rates Since 1945, CRS Report for Congress, 12 December 2012; Paul, Taxation in the United States.

15 Bakija, Tax Policy and Philanthropy, 557.

16 Feldstein, *Economics of Art Museums*, 226-7.

1950s), the charitable deduction provision was of especial benefit to high value estates. In 1942, Congress increased the top rate of Estate Tax to seventy-seven percent, although also raising the standard exemption to \$60,000, where it stood for nearly thirty-five years. However, there was no limit one could bequeath to charity and take a deduction (although there was a limit on income tax).¹⁷ Less well known – but promoted privately by museum curators – was that potential donors could make a bequest against their estate while still alive i.e. retain a “life interest”. This meant the deduction value reduced according to the donor’s age at time of the bequest – for instance, in 1956, for a prospective donor of a work of art valued at \$100,000, the value of the deduction would be \$48,030 if s/he was fifty years old, rising to \$72,630 if aged seventy at the time of the bequest – but donors could retain control of their art during their lifetimes.¹⁸ Over the defined period charitable institutions were quick to pick up on the possible benefits of Revenue Code provisions: for instance, Cornell University as early as its 1919 endowment drive noted that “wealthy individuals would bear only a fraction of the price of gifts they made.”¹⁹ The incentive effect continued, evidenced by the fact that in the 1950s charitable bequests made up forty-eight percent of the largest estates.²⁰

The ideology of “indirect support” via the Tax Code provisions outlined above did have some vital – albeit undoubtedly unintended or even unforeseeable – consequences. First is that the American art market, from its beginnings in the 1920s through to maturity in the 1950s, developed a systemic structure – one which prioritised the social as well as economic capital of wealthy individuals as well as art world professionals. This was very different from the norm in Paris, another key modern art market of the early twentieth century. The French “dealer-critic” system emerged in the late nineteenth century to challenge the Academic system in France, whereby the State had promoted the fine arts via annual Salons of contemporary art.²¹ The key agents in this system were: the commercial dealer-gallerist, who typically adopted the role of “entrepreneurial-patron”; and the art critic, who might either write independently for the art press, or be employed in some form by a dealer-gallerist. The key roles of dealer and critic were to develop an artist’s career and “côte” (art market value), and to act as intermediaries between artist and

17 James W. Quiggle, and John Holt Myers, Tax Aspects of Charitable Contributions and Bequests by Individuals, in *Fordham Law Review*, 28/4 (1959). See also David Joulfaian, The Federal Estate and Gift Tax: Description, Profile of Taxpayers, and Economic Consequences, OTA Paper, U.S. Department of the Treasury, December 1998.

18 Alfred Barr to Richard S Davis, 17 October 1955, Alfred H. Barr Jr. Papers, Archives, Museum of Modern Art. See also T.B. Sherman, Art and Taxes, in *Saturday Review of Literature*, 7 July 1956, 5,6,26; Steven Rodgers, Donate Your Art and Keep it Too: How the Government Subsidizes Art Collections for the Rich and What Congress Can Do About It, in *Southern Illinois University Law Journal* 40 (2015). Available from <http://law.siu.edu/common/documents/law-journal/articles-2015/fall2015/8%20-%20Rodgers%20Comment%20-%20Proof%203%20Pending%20-sm.pdf>.

19 Clotfelter, Federal Tax Policy and Charitable Giving, 31.

20 Clotfelter, Federal Tax Policy and Charitable Giving, 25-29.

21 Harrison C. White and Cynthia A. White, *Canvasses and Careers: Institutional Change in the French Painting World* (Chicago: University of Chicago Press, 1993).

private collector.²² If the French state did play any role in the “dealer-critic” system, it was minor (via the legal status of the main auction house, the Hotel Drouot, as a self-governing body of state officers rather than strictly commercial operation). In contrast to the French duopoly, in New York the art market norm became a tripartite system whose key players were modern art museum, commercial dealer-gallery, and private collector.²³ A question is why, when roles remained much the same as in Paris, i.e. to identify artists from a wider pool (gatekeeping); to support and promote artists via gallery exhibitions or in written form; consumption of art works by collectors – why did the New York art market develop a systemic structure different from the French “dealer-critic” norm? Further, why did the modern art museum play an influential role in the New York art market? That this can be linked to the impact of Revenue Code provisions such as the “charitable deduction” is explained below with reference to one institution: the Museum of Modern Art in New York.

The Museum of Modern Art (MoMA), on its founding in 1929, was representative of how, post 1917, American private institutions were chartered to take advantage of existing tax breaks. What was untypical is the extent to which “indirect support” tax provisions played a part. In 1929 MoMA had no core endowment to underwrite running costs or build a permanent collection and no regular purchase funds. The intention of its founders was that it would rely upon wealthy donors for both. Trustees and others started gifting paintings in 1930, and in MoMA’s first decade the value of art works gifted (\$645,260) was more than ten times the value of acquisitions. Even in the early 1950s the ratio of gifts to purchases was approximately two:one.²⁴ Impacting on such donations were the rules governing gifts of appreciated property. The potential advantages can be seen in a hypothetical case: a collector in the seventy percent tax bracket who had paid \$20,000 for a painting which over the years had risen in market value to \$200,000. If said collector sold the artwork paying capital gains tax of twenty-five percent, this would amount to \$45,000. If, on the other hand, s/he gave the piece to a museum such as MoMA, s/he could claim the full \$200,000 “fair market” value as a deduction, while also avoiding paying capital gains tax on any appreciation.²⁵ This so-called “double incentive” was particularly attractive to high net worth individuals (the majority of private collectors or potential donors), and by the mid-1960s some seventy percent of charitable deductions were taken against gifts of appreciated assets, a good proportion of these artworks or similar. Although taxation was not explicitly mentioned in MoMA’s public relations, MoMA cura-

22 Raymonde Moulin, *The French Art Market—A Sociological View* (New Brunswick, NJ: Rutgers University Press, 1987); Malcolm Gee, *Dealers, Critics and Collectors or Modern Painting: Aspects of the Parisian Art Market between 1910 and 1930* (New York: Garland Publishing, 1981).

23 A. Deirdre Robson, *Prestige, Profit, and Pleasure: The Market for Modern Art in New York in the 1940s and 1950s* (New York: Garland Press, 1995).

24 Alfred H. Barr, Chronicle of the Collections, 1929-1967, in *Painting and Sculpture in the Museum of Modern Art, 1929-1967* (New York: Museum of Modern Art, 1977), 628.

25 Heilbrun and Gray, *Economics and Arts and Culture*, 259. See also J.K. Lasser, How to Raise Money Painlessly: The Good Samaritan and his Tax Deductions, in *Harper’s Magazine*, December 1946, 551; Tracy, *Charitable Gifts of Appreciated Property*, 714 ff.

tors such as Alfred H. Barr Jr, as well as New York art dealers, privately informed collectors of the potential benefits of the provisions, particularly after top marginal tax rates were raised in 1951 and the above deduction exemption increased to twenty percent (1952) and then thirty percent of AGI (adjusted gross income) in 1954, though the top rate of Estate Tax remained steady at seventy seven percent from 1942 to 1976.²⁶ Indeed, a number MoMA trustees and other donors gave quite significant groups or whole collections to the museum: for instance, in 1953 pioneer collector-patron Katherine Dreier, in dividing her collection between several museums, left MoMA 102 early twentieth-century works, while, over the years, Trustee Nelson Rockefeller gifted MoMA more than twenty-five works.²⁷

The reliance of MoMA upon wealthy donors raises the issue of private collectors’ role within the New York art market system. Conventionally, as Belk notes, art collecting is not only “socially sanctioned as a legitimate and worthwhile activity which provides collectors with a noble sense of purpose,” it serves to memorialise a collector’s social status and valorise their “cultural capital.”²⁸ Moreover, Revenue Code provisions mean that private donors potentially have considerable influence upon charitable organisations: not only did “American tax law in effect recognize[d] that donations replace government spending and, by extension, give legitimacy to the social value of donor’s preferences”.²⁹ Moreover, “large gifts [also] open[...] the door to forms of philanthropy in which donor control is inherent.”³⁰ At its most extreme, the suspicion is that the wealthiest donors find institutions from which they can benefit and over which they can assert control. Private individuals could, if they so desired, impact not only upon museum direction but, by implication, the commercial status of art, in this case European and American modern art. Some collectors associated with MoMA surely did seem to share such ambition. This was bluntly expressed by a founding trustee of MoMA in 1930: “We only want the works of men owned by the Trustees. That’s the only way we can run this Museum.”³¹ This statement was made with respect to temporary exhibitions, but is surely relevant to the shaping of the museum’s collection in subsequent years: the Acquisition Committee was controlled by Trustees.

The above does not necessarily suggest an impact of the Revenue Code on the New York *market* for modern art. However, over the years, MoMA assumed special standing as a key player in the New York art market. Foregrounding the “provocative spectacle of the thickest pillars of conservative society” – the founding trustees – as “upholding a

26 Feldstein, *Economics of Art Museums*; Joulfaian, *The Federal Estate and Gift Tax*.

27 *Bulletin of the Museum of Modern Art*, 1953; B. Gold, *Nelson A Rockefeller Collection: Modern Works at MoMA*, in *Arts*, XLIII/7, 28-30; *Twentieth Century Art from the Nelson Aldrich Rockefeller Collection*, Museum of Modern Art (New York, NY), 1969.

28 Russell W. Belk, *Collecting in a Consumer Society* (London: Routledge, 1995), 76.

29 Clotfelter, *Charitable Giving and Tax Policy in the U.S.*, 4.

30 Odendahl, 1990, cited in Auten et al, *Taxes and Philanthropy Among the Wealthy*, 401.

31 Russell Lynes, *Good Old Modern: An Intimate Portrait of the Museum of Modern Art* (New York: Atheneum, 1973), 71.

distinctly radical artistic cabal ... not merely with cash but also with vigorous personal effort” helped give social cachet to modern art as well as to MoMA itself.³² Encouraging modern art collecting was a key concern of Alfred Barr, MoMA’s Director of Collections. One means for this was special exhibitions of works owned by trustees and other private collectors. Furthermore, in a very novel way Barr, as early as 1934, suggested promoting modern art as fiscally advantageous, mentioning “businessmen who may not be interested in modern pictures but who certainly are interested in an increase in value of 200,000 per cent.”³³ To this end, museum press releases and articles in mainstream periodicals were used to emphasise increases in art market values of artists and works in the Modern’s permanent collections as “a record of rewarding speculation, backed by some brilliant hunches and rare streaks of luck.”³⁴ MoMA’s success of promoting links between modern art and market values can be seen in increasing discussions of modern art and its market in the American business press in the mid-1950s. By the late 1950s “the buccaneer investor who does not know what he likes but knows a good investment when he sees one” was for the first time noted as a presence in New York.³⁵ MoMA’s efforts to encourage the market for modern art resulted in it being seen by the 1950s as a seminal player in the New York art market and, according to curator Andrew Ritchie: “the Bourse. Everything we did the dealers knew about it before we did it, and prices were affected accordingly.”³⁶

That MoMA was indeed the “Bourse” can be inferred from art market performance in the post-war years. The stars of MoMA’s first exhibitions, and early collection were Post-Impressionist painters: by the late 1940s it was considered almost impossible to find such paintings of any quality for less than \$10,000, and “museum quality” pieces could cost much more. By the late 1950s, against a decade of American economic prosperity and low inflation, characteristic prices in New York for major Impressionist and Post-Impressionist paintings was reported as being up to high five-figure to mid-six-figure sums.³⁷ The success of MoMA’s efforts surely played a part in this: “blue chip” market values shadowed MoMA’s exhibition and collection priorities, particularly in its first decades. Rising prices were also aided and abetted by an increasing scarcity of “museum quality” pieces: the taxation policies cited above, and the ostensible legal status of works donated to museums, helped create a drift of art into institutional collections, particularly of the art and artists critically validated by museums.³⁸ In the case of French “classic” modern

32 The Museum of Modern Art, in *Fortune Magazine*, December 1938, 127.

33 Barr, qtd. in Dwight MacDonald, Action on West Fifty-Third Street II, in *The New Yorker*, 19 December 1953, 52.

34 The Big Gamble, in *Vogue*, 1 November 1954, 106.

35 Under the Boom, *Time*, 1958, 66. See also Eric Hodgins and Parker Lesley, The Great International Art Market II, in *Fortune Magazine*, January 1956, 122-136.

36 Qtd. in Lynes, *Good Old Modern: An Intimate Portrait of the Museum of Modern Art*, 250.

37 Robson, *Prestige, Profit, and Pleasure*, 228-9, 238-39.

38 Karl E. Meyer, *The Art Museum: Power, Money, Ethics (A Twentieth Century Fund Report)* (New York: William Morrow and Co. Inc, 1979); Marie C. Malaro, Deaccessioning: The American Perspective, in *Museum Management and Curatorship*, 10 (1991), 273-279.

art, New York shortages of major works were exacerbated by the fact that post-war the French State began severely to restrict the export of French artworks.³⁹ Further, when the “best works by the great veterans of the modern movement ... move[d] beyond the average collector’s reach”⁴⁰ private collectors typically seek alternative foci, with the consequence of successive waves of price rises. The “classics” of early twentieth century modernism as promoted by MoMA’s exhibition schedule and collections – for instance Matisse and Picasso – were reported as fetching low five figure sums by the late 1940s, and by the mid-1950s major works by the same painters could fetch the high five or even low six-figure sums that had been associated with Impressionism and Post-Impressionism five to ten years previously.⁴¹ Another example of collectors shifting from one focus to another when prices escalate was American post-war abstract painting, somewhat controversially promoted in MoMA’s post-war exhibition schedule. The market value for “museum quality” examples of such painting, particularly by best known names such as Jackson Pollock, rose ten-fold in the 1950s: from high three-figure to very low four-figure sums for his largest paintings circa 1950, to five-figure sums for “museum quality” works by the late 1950s.⁴² Interestingly, this rise in prices was entirely due to growing local demand for this art, reflecting the now mature status of the New York modern art market.

From the stand-point of the twenty-first century, one might expect such market trends to encourage some American collectors to consider the sales potential of their collections (in whole or part) as a way of valorising their acumen (whether aesthetic or financial). The only easily verifiable arena is the public auction sale, with the potential of public sales prices – and press coverage of the same – an indicator of the success of MoMA’s strategy of encouraging an interest in the investment potential of modern art. Indeed, New York auction house grosses doubled in the later 1950s to \$10.2 million in 1959, due largely to two significant sales in 1957-58: expatriate French collector Georges Lurcy’s collection in November 1957, which totalled \$1.7 million; and that of American hotelier Arnold Kirkeby’s collection in November 1958.⁴³ The Kirkeby sale in can help elucidate why auction sales did not offer the best way for wealthy private collectors to manage their collections. Kirkeby was presumably encouraged by escalating prices for Impres-

39 James Thrall Soby, memo to Alfred H. Barr, 27 November 1949, Alfred H. Barr Jr. Papers, Archives, Museum of Modern Art.

40 James Thrall Soby, *The State of Collecting*, in *Saturday Review of Literature*, 2/08/1952, 38.

41 Robson, *Prestige, Profit, and Pleasure*, 237-241.

42 *Ibid.*, 233-34, 248-49.

43 Art Market Untouched by Recession, in *Arts*, September 1958, 11; Richard H. Rush, *Art as an Investment* (Englewood Cliffs NJ: Prentice Hall, 1961); Wesley Towner, *The Elegant Auctioneers* (New York: Hill and Wang, 1970); Eric Hodgins, and Lesley Parker, The Great International Art Market II, in *Fortune Magazine*, January 1956, 122-136; S. Knox, Modern Art Brings Record \$1,708,550, in *The New York Times*, 8 November 1957, 1; Peak in the Masterpiece Market, in *Life Magazine*, November 1957, 145; Aline Saarinen, Auction of Art Brings \$1,548,500, in *The New York Times*, 20 November 1958, 1, 32; Aline B. Saarinen, A Seller’s Market, in *The New York Times*, 23 November 1958, II13.

sionist and Post-Impressionist paintings in New York and in Paris, and in realising \$1.5 million for thirty “classic” modern French paintings, seemed to have made an astute decision, even though he would have been liable for twenty-five percent capital gains tax, as levied in the United States in the 1950s and 1960s, on the proceeds. However, not only were auction sale values in New York lower than equivalent sales in Europe but, as art market insiders and fellow collectors would have been aware, prices realised at the Kirkeby sale were also not “fair market value”: for instance, the \$152,000 sale price for Picasso’s *Mother and Child* (1903) was substantially lower than the \$185,000 Kirkeby had paid a Fifty-Seventh Street dealer in 1957.⁴⁴ Valorising one’s collecting acumen – or investment potential – via a public auction proved not to be a recommended option in New York, and gifting works from private into museum collections remained the default option. The significance of this will be appreciated when comparing 1950s art market patterns – framed by the above-described tax preferences – to those of the 1980s.

The period discussed above coincides with, as noted above, an ongoing national consensus about the benefits and equity of progressive taxation, alongside the emergence and then coming-of-age of the New York art market (both in terms of systemic structure and growing art market activity). To further consider the impact upon the New York art market of Federal taxation, an interesting counterpoint is the 1980s. The rationale for this is two-fold. One, to which we will return later, is that this decade witnessed a new exuberance for the New York art market, after a decade of relatively weak performance both in market volume and recorded sales prices. Second is that the 1980s was a period of unprecedentedly radical tax reforms. The 1981 Economic Recovery Act (ERTA) and 1986 Tax Reform Act (TRA86) were informed by 1970s supply-side economic theory, and strongly committed to taxing all economic income uniformly to stimulate economic performance following a decade of stagflation.⁴⁵ Tax reform was facilitated by President Reagan’s enthusiasm for reforming a tax system seen as “unwise, unwanted and unfair,” and making it more equitable by eliminating complexity and tax loopholes.⁴⁶ First, the 1981 ERTA significantly reduced the top marginal income tax rate from seventy percent to fifty percent, and also reduced the top rate of estate tax from seventy to fifty percent. The TRA86 extended ERTA by reducing individual tax rates from the previous multiple graduated brackets to four bands (including a top marginal rate of twenty-eight percent, plus a thirty-three percent band reflecting a five percent surcharge to be paid by the top income taxpayers), accompanied by a complicated series of structural amendments to

44 Expensive Apples, in *Time*, 24 June 1957, 68; 7 Paintings Sold for \$2,186,800, in *The New York Times*, 16 October, 1958, 1,41; Alfred Frankfurter, Midas on Parnassus, in *ArtNews Annual XXVIII*, November 1958, 54.

45 Charles E. McLure, Jr., The Political Economy of Tax Reforms and their Implications for Interdependence: United States, in *The Political Economy of Tax Reform*, NBER-EASE Vol.1 (University of Chicago Press, 1992); Charles H. Stewart III., The Politics of Tax Reform in the 1980s, in Alberto Alesina and Geoffrey Carliner, eds., *Politics and Economics in the Eighties* (Chicago: University of Chicago Press, 1991).

46 Jeffrey H Birnbaum; Alan S Murray, *Showdown at Gucci Gulch: Lawmakers, Lobbyists, and the Unlikely Triumph of Tax Reform* (New York: Vintage Books, 1988), 95, 286-87. See also: Stewart, The Politics of Tax Reform in the 1980s; and McLure, The Political Economy of Tax Reforms.

reduce tax deductions and loopholes.⁴⁷ The TRA86 also extended the Individual Alternative Minimum Tax (AMT) first introduced in 1969 – a surcharge tax on high-income households, equal to ten percent of the sum of tax preferences in excess of \$30,000, plus the taxpayer’s regular tax liability. This was because in 1969 there had been concerns that, with marginal rates as high as seventy percent, gifts of highly appreciated assets could result in \$1.19 of tax savings – a paper profit – for the dollar value of a donation, concerns which were still being publicised in 1986. More particularly, the new extended AMT introduced a particularly unfavourable treatment for the gifting of appreciated assets: the “double incentive” of “fair market value” on appreciated assets and forgiveness of capital gains tax was eliminated, and only the original “cost” could be taken.⁴⁸ The reduction of income tax rates was accompanied by equalising the top marginal tax rate and capital gains tax at twenty-eight percent. This was the first time both tax rates had been the same since 1945, the latter having been twenty-five percent for many years pre-1965, before being reduced to twenty percent in the early 1980s.⁴⁹

There is no obvious evidence that legislators thought at all about how fiscal changes might impact upon “indirect support” for the arts, despite the fact that for some commentators “it is not hard to see” how changes to tax rates, and related provisions, might impact on charitable giving.⁵⁰ Ostensibly, it might have seemed that an increase in capital gains tax and reduction in income tax marginal tax rates might combine to make charitable gifting of appreciated property more attractive. Indeed, initially, 1980s commentators thought it plausible that the strong tradition of “giving away thirty-cent dollars” developed between 1965 and 1980, when the marginal rate of tax had never been less than seventy percent, was so ingrained it would continue.⁵¹ However, as Feld notes: “Tax changes that work to the advantage of taxpayers by decreasing their taxes work to the disadvantage of charitable institutions.”⁵² Indeed, the wealthiest proved particularly change sensitive: whether to the “price” of giving \$1 in cash rising from thirty to fifty cents for the highest income group in 1981; the more than doubling to sixty-two cents in the dollar for those in the highest tax bracket (\$500,000 p.a. plus) in 1986; or that, post-1981, the reduction of the top rate of estate tax from seventy to fifty percent meant the

47 Charles T. Clotfelter, *The Impact of Tax Reform on Charitable Giving: A 1989 Perspective*, NBER Working Paper #3273, (March 1990); Stewart, *The Politics of Tax Reform in the 1980s*.

48 Auten et al., *Taxes and Philanthropy Among the Wealthy*, pre-publication typescript, 13-14; McLure, *The Political Economy of Tax Reforms*, 103; Wolff, qtd. in Clotfelter and Ehrlich, *Philanthropy and the Nonprofit Sector in a Changing America*, 219; Fullerton, in Feld, *The Economics of Art Museums*, 208; Clotfelter, *The Impact of Tax Reform on Charitable Giving*.

49 Birnbaum and Murray, *Showdown at Gucci Gulch*, 4.

50 Clotfelter, *Charitable Giving and Tax Policy in the U.S.*, 9. See also Robert Pear, *The Tax Bill and Arts Patronage*, in *The New York Times*, 17 June 1986.

51 Leonard Sloane, *Your Money: Charitable Gifts and Tax Law*, in *The New York Times*, 6 June 1987. Available at: <https://www.nytimes.com/1987/06/06/business/your-money-charitable-gifts-and-tax-law.html>.

52 Feld et al, *Patrons Despite Themselves*, 181.

“price” of bequests significantly increased.⁵³ Moreover, the TRA86 extension of AMT meant that “for some potential gifts, ... [it] had the effect of virtually wiping out the bulk of the deduction, particularly of artworks.”⁵⁴ For instance: if donating appreciated property worth \$10,000, with an original cost of \$8,000, the value of the exemption pre-1986 would have been \$5,400 (\$5,000 from the deduction at a fifty percent marginal tax rate plus \$400 from the forgiveness of capital gains tax at twenty percent); under the new rules, the value of the exemption fell to \$3,360 (\$2,800 from deduction at the twenty-eight percent top tax rate, together with a liability for \$560 capital gains tax at the twenty-eight percent rate).⁵⁵ The 1980s reforms, more particularly the expanded AMT, quite quickly depressed charitable contributions, more particularly gifts of artworks to museums from the wealthiest collectors. Between 1986 and 1988, Rosett notes a fall of fifty-four percent in such donations; in 1987 the American Association of Museums estimated that 162,000 fewer objects had been donated than in the previous year; while a 1989 study by the Association of Art Museum Directors found that “the value of donations [to art museums] declined by \$161 million or sixty-three percent, from 1986 to 1988 for the 116 institutions reporting.” In the same two-year period MoMA reported a fifty-eight percent fall in donations; the Metropolitan reported a decline of sixty-six percent, with gifts of significant value virtually at a stand-still unless the donors were fulfilling long-term commitments; while the St Louis Art Museum reported a fall in donation values from \$1.75 million in 1986 to \$349,000 in 1988.⁵⁶

In the 1980s major American collectors seem to have begun to re-assess how they might dispose of their collections, something which at mid-century would seem to have been gifting to an art museum of choice. They did this against the “Reagan boom” of the mid-1980s, the tax reforms outlined above, and the re-emergence of a buoyant New York art market after the post-1973 sluggishness of the decade. The period 1980-1990 witnessed record-setting prices for both “classic-modern” painting and post-war contemporary art. In 1980 total art dispersals at Sotheby’s and Christie’s New York totalled \$147 million; in 1987-88, auctions of modern art in New York totalled nearly \$85 million in sales. The ultimate records for modern art were set by two Van Gogh paintings – *Iris*es and *Portrait of Dr. Gachet* which sold at auction for \$53 million and \$82.5 million respectively.⁵⁷ The dec-

53 Wolff in Clotfelter and Ehrlich, *Philanthropy and the Nonprofit Sector*, 219; Clotfelter, *The Impact of Tax Reform on Charitable Giving*; Fullerton, *Tax Policy Toward Art Museums*, 206-208; Bakija, *Tax Policy and Philanthropy*, 562-563.

54 Fullerton, *Tax Policy Toward Art Museums*, 208.

55 Clotfelter, *Charitable Giving and Tax Policy in the U.S.*, 8.

56 Liegel, *Impact of the Tax Reform Act of 1986 on Lifetime Transfers of Appreciated Property for Conservation Purposes*, 742-797. Feldstein, *The Economics of Art Museums*, 168; Grace Glueck, *Donations of Art Fall Sharply After Changes in the Tax Code*, in *The New York Times*, 7 May 1989, 32; Daniel Grant, *Record Prices, Tax Reform Brings More Artworks to Auction*, in *Baltimore Sun*, 4 December 1988, G4; Robert Pear, *The Tax Bill and Arts Patronage*, in *The New York Times*, 17 June 1986; C. Twardy, *Tax Law Has Art on the Auction Block, Not on Display*, in *Orlando-Sentinel*, 18 June 1989, available at http://articles.orlandosentinel.com/1989-06-18/lifestyle/8906180112_1_american-museums-museum-in-new-art-museum-directors.

57 Rita Reif, *How Auction Sales are Transforming the Art World*, in *The New York Times*, 27 July 1980, 2/1; Katrine Ames, Maggie Malone, and Donna Foote, *Sold! The Art Auction Boom*, in *Newsweek*, 18 April 1988.

ade also saw a marked escalation in the prices of post-war living artists: Jasper Johns's *False Start* fetched \$16.5 million in New York, four times the original estimate. Even more remarkable was the 10,000-fold increase of sale price for a David Hockney painting sold for \$200 in 1961, which was appraised at \$20.5 million in 1989.⁵⁸ Most record auction prices followed the October 1987 Stock Market Crash, and were seen as in large part due to the entrance of “brash” Yuppie American collectors inspired by the ethos of the Reagan boom, together with a significant Japanese presence: it was a Japanese collector who paid the record sum for *Dr Gachet*, while Japanese buyers were estimated to be one-third of top-flight buyers at this time.⁵⁹ For Ardenne the reasons for the New York art market boom were: “triumphant free-marketism, producer of inflated fortunes and rapid accumulation of wealth ... [...] accompanied by homage to the present ...” – an art market which drew strength not from scarcity but availability.⁶⁰ This speculative bubble collapsed in early 1991 when it was revealed that much Japanese buying had been a front for widespread corporate fraud and tax avoidance.⁶¹ In the early 1990s the New York art market was noticeably sluggish, even if for some it seemed more of a “correction” than a slump.⁶²

The above developments puzzled contemporary commentators who found themselves at a loss satisfactorily to explain art market behaviour in the later 1980s, particularly the fact that the art market did not mirror the Stock Market Crash of 1987, as might have been expected in light of the historical examples of 1929 and 1973.⁶³ However, what was not factored in was the possible impact of the tax reforms of 1981 and 1986. Two New York auction sales exemplified the impact of tax reforms, and more especially the extension of AMT in TRA86. The first was a sale of the bluest of “blue chip” European modern paintings, which by the 1980s had been drifting into American museums from mid-century onwards (as per the history of MoMA's collections), with consequences for scarcity value as well as critical prestige; the second was a sale of the post-war American abstract art whose critical status had been promoted by MoMA from the 1950s, and which attracted some of the highest prices in the 1980s boom. The former sale, at Sotheby's New York in November 1987, included work consigned by John Whitney Payson, who had decided to sell Impressionist and Post-Impressionist paintings inherited in 1975 from his mother, wealthy art collector Joan Payson Whitney (owner of the New York Mets baseball team) who had started collecting in the 1950s. Until this decision Payson had been expected to donate the twenty-eight paintings he inherited to Westbrook College in Portland, Maine,

58 Paul Ardenne, The Art Market of the 1980s, in *International Journal of Political Economy*, 25/2 (Summer 1995), 108-109.

59 Ardenne, The Art Market of the 1980s; Emily L. Diamond, A New Era: An Analysis of the Contemporary Art Market Bubble, M.A. thesis, Harvard Extension School, 2016; Peter C. T. Elsworth, All About/Art Sales: The Market's Blue Period, in *The New York Times*, 10 May 1992.

60 Ardenne, The Art Market of the 1980s, 111.

61 Elsworth, All About/Art Sales.

62 Peter C.T. Elsworth, The Art Boom: Is it Over, or is this Just a Correction?, in *The New York Times*, 16 December 1990.

63 Ardenne, The Art Market of the 1980s, 110.

where they had been on loan for ten years. The decision to sell rather than donate attracted press attention; the sale itself attracted headlines because Van Gogh’s *Iris*es went for a record-breaking \$53.9 million (about twice the pre-sale estimate).⁶⁴ Recent very high auction prices in New York for Van Gogh surely were a factor in Payson’s decision to sell, but the new AMT restrictions also played a key part. Payson, in justifying the sale, calculated that pre-1986 a work of art acquired for \$10,000 which had increased in value to \$100,000 would have brought a \$50,000 tax savings if donated to a museum or other charitable institution, whereas in 1987 “that art work would bring a tax benefit of only \$2,100.”⁶⁵ Payson may have been exaggerating, but instead of being able to claim a deduction at “fair market value” (equal to the pre-sale estimate of some \$26 million), he would only have been allowed “cost” of \$1.8 million, the value of the work when he inherited it. The sharply higher “price” of giving – more than doubled to seventy-nine cents, relative to thirty-one cents pre-1981 – would also have applied to sales of post-war abstract American art, as for instance when Burton and Emily Tremaine decided to dispose of their collection in the mid-1980s. The Tremaines had begun collecting in the 1950s, typically buying new artists and styles early and adventurously, when market values were low; by the mid-1980s they had built an unambiguously “museum quality” collection, and had previously given works to the National Gallery in Washington D.C. and Wadsworth Atheneum.⁶⁶ There were two Tremaine sales: the first in 1988 after Emily’s demise; the second in 1991 after Burton’s death. The 1988 sale seemed to vindicate the decision to sell: it occurred at the peak of the late 1980s art market boom and set records for post-war American abstract art, including \$7.04 million for Jasper John’s *White Flag* (1955-8).⁶⁷ Emily’s given reason for selling was “control” over her “legacy,”⁶⁸ but for a collector who in the 1970s stated her excitement at post-war American artists selling for high prices, the impact of tax reforms such as AMT’s particularly unfavourable treatment of appreciated assets must be factored in. Indeed, the pre-1986 deduction for “fair market value” of a major Johns might have been expected to be around the \$1.76 million

64 Rita Reif, Van Gogh ‘Iris

65 Dealer Selling Van Gogh to Support Arts in Maine, in *Orlando-Sentinel*, 5 September 1987; Rita Reif, Tax Law and Art Gifts.

66 Kathleen L. Housley, *Emily Hall Tremaine: Collector on the Cusp* (New York: Emily Hall Tremaine Foundation, 2001); *The Tremaine Collection: 20th Century Masters – The Spirit of Modernism*, Wadsworth Atheneum, Hartford, Connecticut, 1985; *The New York Times*, 1991.

67 Judd Tully, Rosenquist Work Sold for \$2.1 Million, in *The Washington Post*, 12 November 1986; Rita Reif, Christie’s to Auction Works from Two Art Collections, in *The New York Times*, 8 September 1988; Rita Reif, 50 Paintings to be Sold from Tremaine Estate, in *The New York Times*, 7 June 1991.

68 Housley, *Emily Hall Tremaine: Collector on the Cusp*, 215; Emily Tremaine, interview with Paul Cummings, 24 January 1973, Oral History Collection, Archives of American Art, Smithsonian Institution, Washington D.C.

paid at auction in 1986 for *Double Flag* (1962); post-1986, the Tremaines could have only claimed “cost” i.e. the approximately \$1000 paid in 1958.⁶⁹

The Federal tax system is known for being very complex, and riddled with loopholes, which the attempts at tax reform did not eliminate. The seeming disavowal of the previous convention of gifting works to a museum (while at the same time taking a tax break) by the collectors above was not the whole story. In selling their collections at auction both Payson and the Tremaines made use of an alternate sophisticated form of tax preference: the private foundation. Contributions to private foundations continued to be fully deductible and, despite some restrictions, allowed transferees to control how their donations were used. By 1961 it was estimated that the wealthiest typically held some thirty percent of their assets in private foundations, while some families such as the Rockefellers established multiple foundations.⁷⁰ In 1987, Emily Tremaine set up a private charitable foundation, and it was to this the proceeds of the 1988 (after Emily’s death) and 1991 auction sales (after Burton Tremaine’s decease) went. This surely enhanced the attractiveness of selling post-AMT. Payson also used this tax break in gifting twelve and a half percent of proceeds from the sale of *Irises* to establish the “Joan Whitney and Charles Shipman Payson Charitable Foundation,” in honour of his parents.⁷¹ What was novel was to set up private foundations from monies realised by public auction sales, rather than using foundations to protect existing capital.

The hope is that it has become clear that Federal taxation, and more particularly changes in rates and exemption provisions, did indeed have some impacts, presumably unintentional on the part of legislators, upon the development of the market for modern art in the United States in the two periods discussed (mid-century between the 1930s and 1950s, and the 1980s). The 1980s reforms were not, however, the end of the matter with respect to the impacts of Federal tax preferences and reforms upon the art market. If 1988 (the first full year when unfavourable AMT treatment was in effect) saw a fall of donations of art works to only sixty-four percent of preceding years, there were some developments subsequently. Due to intensive lobbying of Congress, the “fair market-value” deduction was quite quickly restored, and average gift levels in 1991-1992 were approximately ninety percent higher than in 1988-1990. When the unfavourable AMT treatment was re-imposed in 1992, the donation rate again fell sharply. Only when the “fair market value” provision was permanently restored in 1993 did donation levels rebound again, albeit less sharply than before.⁷² The latter changes coincided with a slump in the New

69 Titia Hulst, *The Right Man at the Right Time Leo Castelli and the American Market for Avant-Garde Art*, PhD dissertation, New York University (2014), 176.

70 Ferdinand Lundberg, *The Rich and the Super-Rich: A Study of the Power of Money Today* (London: Nelson, 1969), 160-61; Auten et al, *Taxes and Philanthropy Among the Wealthy*, pre-publication typescript, 9.

71 Housley, *Emily Hall Tremaine: Collector on the Cusp*, 215; *Dealer Selling Van Gogh to Support Arts in Maine*, in *Sun-Sentinel*, 5 September 1987.

72 Susan F. Rasky, *Senate Panel Adopts Tax Change on Gifts of Art and Manuscripts*, in *The New York Times*, 16 Oct. 1990, B8; Irvin Molotsky, *Tax Break to Aid Museums*, in *The New York Times*, 19 August 1993, Section C, 11; Auten et al, *Taxes and Philanthropy Among the Wealthy*, pre-publication typescript, 24.

York art market, which may have had some impact on these figures. However, marginal tax rates remained much the same, and the “price” of giving remained high in comparison to previous decades. Bakija, surveying income-tax data between the 1970s and 2000s, notes that in the 1970s high-income Americans (with incomes over \$500,000 in 2007 dollars) gave around twice as much to charity than in 2007, when the top tax rate was thirty-five percent.⁷³ The reduction in rates of charitable donations generally, and art works in particular (noted as being disproportionately high among the very wealthiest), surely signals a diminution in the previous near-inevitable drift of major artworks into museums. How tax impacts on the art market is not static: a recent trend is the founding of private art museums as private foundations, which raises some new – and persistent – questions as to the relation of this to the tax system.⁷⁴ However, this is not the place to explore the post-1980s market for modern art and its relationship to fiscal questions. In conclusion, the impact of Federal tax codes, and reforms may be said to have had a noticeable impact in the twentieth century – first with respect to helping shape the systemic structure of the New York market for modern art at mid-century, and secondly, in connection to the 1980s tax reforms which shifted collector priorities. But as long as tax preferences are central to the Federal Tax Code, it seems likely that there will be impacts not just upon the arts world more generally but upon the *market* for modern art more particularly.

Deirdre Robson is Senior Lecturer at the London School of Film, Media and Design, University of West London.

73 Bakija, Tax Policy and Philanthropy, 560-566.

74 E. Alex Kirk, The Billionaire’s Treasure Trove: A Call to Reform Private Art Museums and the Private Benefit Doctrine, in *Fordham Intellectual Property, Media and Entertainment Law Journal*, 27/4 (2017), 869-933. See also Grace Glueck, When Collecting Whets the Appetite for a Museum of One’s Own, in *The New York Times*, 6 April 1986, 2:33; Patricia Cohen, Writing Off the Warhol Next Door, in *The New York Times*, 10 January 2015, BU1; Evan Fallor, Hatch Probes Tax-Exempt Private Museums, in *The Bond Buyer*, 1 (6 March 2016).