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Fine Art Capital Rides Art Wave



Liz Peek

Andy Augenblick has an 89-year-old client who has, to put it politely, outlived his liquidity. He is not broke exactly, but on the other hand, he has no cash. What he does have is an important painting, valued at many millions of dollars.

The client has several choices. He can sell the painting today and live off the proceeds for years to come. Or he can borrow against the painting, in effect taking out a reverse mortgage that will pay him a monthly income for the rest of his life.

Here's why the decision is an easy one. Because the government sees no economic advantage to encouraging people to hold onto their Picassos, the capital gains tax on art and antiques was never reduced, and remains at 28%, not 15%. Throw in local taxes, and the 20% commission due an auction house, and the proceeds from selling the painting are sliced in half. Not an attractive solution.

On the other hand, the client can borrow from Mr. Augenblick's company, Fine Art Capital, and keep the painting, which will find its way into the client's estate. The heirs will pay inheritance taxes, but they would have paid them on the remaining cash proceeds in any case. They avoid the capital gains haircut, since it will have been marked to present value when taken into the estate. They can then sell the picture, incurring only the sales commission.

These are the kinds of issues that

Fine Art Capital deals with on a daily basis. This outfit lends against fine art and antiques, occupying a narrow but increasingly popular niche in the financial services business. There are few players in this arena because the specialty requires not only banking expertise but also an ability to analyze artworks dispassionately and determine their value as collateral.

This is no mean feat, as the firm makes loans against paintings and sculpture, in addition to financing collections of rare coins, antique rugs, vintage wine, stringed instruments, Chinese porcelains, Georgian furniture, and other items of similar value and rarity. Fine Art Capital has mastered this challenge by employing several experts who formerly worked at auction houses Sotheby's and Christie's.

It is not wholly accidental that Mr. Augenblick is not only a financier, but also a major collector of museum-quality English furniture and contemporary art. His interest in founding the business stemmed originally from having inexpertly disposed of one of his own valuable paintings. Faced with a huge tax bill, he realized that art as an asset class was underserved, in that it did not have a related debt market. At the time, he had recently retired from his day job, so to speak, as president and co-owner of the Related Cos. He was also bored.

To finance the venture, he teamed up with Emigrant Savings Bank and opened Fine Art in 2004. While there are a few other art advisory businesses, including a unit

of Citigroup, Fine Art has carved out a solid niche. The company does not do appraisals or advisory work and does not help clients dispose of property. It is simply a lending institution, making loans that usually range from between \$3 million and \$20 million, with durations of up to 20 years.

To Mr. Augenblick, the evolution was natural. "People statistically own art longer than they own their homes," he says. "They don't want to have to upgrade as they acquire wealth. They want to buy the best there is. Also, people like hedge fund managers don't want to take money out of their funds. That looks bad to clients. So we can lend them money for acquisitions."

The company works with individuals, museums, art dealers, and estates. The business is seasonal. During the spring and fall auction seasons, the company is busy assisting those looking to finance purchases. This is typically done through issuance of a letter of credit. Prospective buyers typically do not want to sell assets, especially near yearend, to finance purchases.

Estate clients share a common problem. Because estate taxes have to be paid within nine months of a person's death, the heirs may have only one auction season in which to dispose of art or antiques. This sets up a possible "fire sale," which can be avoided by taking out a loan against the property and waiting for a more propitious time to sell.

According to Mr. Augenblick, the art world has become somewhat more transparent. More works are flowing through auction houses,

and information about sales and prices is obtained easily online. That's good news for investors, but not such great news for heirs. The old trick of walking off with mom's paintings doesn't fly anymore. The Internal Revenue Service has become increasingly vigilant about checking the provenance of works that come up for auction, and comparing that with estate records.

Consequently, estates are taking greater care to record artworks, and also to maximize their sales values. This is a major opportunity for Fine Art Capital. "There's over \$1 trillion of art in private hands," Mr. Augenblick says. "Over the next 20 to 30 years, a significant percentage will change hands."

Fine Art is riding a wave of escalating prices in the art world. Rising values give people and institutions the confidence to borrow against purchases, and encourage people to deal with their artwork in a sophisticated manner. Mr. Augenblick is optimistic that many categories of art still have appreciation potential. While there are some categories that he might steer clear of — such as antiquities, where provenance issues have created problems for the Metropolitan Museum of Art and the J. Paul Getty Museum — he sees no huge bubble about to burst on the art scene. So far, the company has never had a default.

Unlike many successful people who show off their collections on the walls of their office, Mr. Augenblick keeps his art in his home and in storage. "We don't want clients to think we've been foreclosing," he says.

peek10021@aol.com