STEPHENSON HARWOOD

Art and cultural property

In this issue:

Welcome to the latest issue of our "Art law - recent developments" newsletter in which we discuss legal issues currently affecting the global art community.

In this issue we look at:

- Art market regulation – Recent AML and financial crime developments
- France's mixed canvas: the country's incomplete efforts towards the restitution of looted art
- The cultural heritage sector's originality question – Impact of *THJ v Sheridan*
- Art – is it worth considering structuring?

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Art market regulation - Recent AML and financial crime developments

Introduction

Tackling economic crime has moved to the top of the UK political agenda, with a key focus on combatting fraud. The publication of *the Economic Crime and Corporate Transparency Act 2023* at the end of last year brought in robust new laws and enforcement strategies to fight fraud, counter corruption and bolster legitimate interest and, showcases the Government's intention to make the UK the hardest place in the world for economic criminals to operate.

The Global Art Market has for some time, been seen as a "high-risk industry" for money laundering and terrorist financing. Indeed, in February 2023, the Financial Action Task Force published a report in which it categorised the Global Art Market as one which has historically "*attracted criminals, organised crime groups and terrorists seeking to launder the proceeds of crime*". In line with this, regulatory scrutiny of the Art Market in the UK is tighter than ever with an enhanced emphasis placed on identifying and raising awareness of the inherent risks within the Art Market and improving the safeguards put in place by Art Market Participants to mitigate against these risks. In January, the National Crime Agency issued an Amber Alert on *Financial Sanctions Evasion, Money Laundering & Cultural Property Trafficking Through the Art Storage Sector* (available here).

In this Article, we look at the key updates to the regulatory landscape which Art Market Participants need to be aware of in order to ensure they, and their businesses, have the requisite policies and procedures in place to meet the relevant laws and regulations.

Updates to BAMF Guidance

The UK Money Laundering and Terrorist Financing Regulations 2019 took effect on 10 January 2020 (the "**Regulations**") and brought the Art Market into the scope of the Money Laundering Regulations 2017 (the "**MLRs**") (as amended) via the introduction of the concept of Art Market Participants ("**AMPs**"). For the purposes of the Regulations, AMP is defined as:

"*A firm or sole practitioner who by way of business trades in, or acts as an intermediary in the sale or purchase of, works of art and the value of the transaction, or a series of linked transactions, amounts to 10,000 euros or more*".

Shortly following the publication of the Regulations, the British Art Market Federation ("**BAMF**") published sector specific guidance, approved by HM Treasury, to assist the Art Market in understanding their responsibilities under the MLRs (the "**Guidance**"). The Guidance has been updated twice since its original publication with the most recent version being published on 6 February 2023.

In accordance with the provisions of the MLRs, AMPs are required to conduct customer due diligence measures ("**CDD**") on customers to: (i) identify the customer; (ii) verify the customers identity; and (iii) assess the purpose and intended nature of the business relationship or occasional transaction with that customer.

The definition of "*customer*" for the purposes of AMP's requirements under the MLRs has evolved since the original publication of the Guidance. Under the original Guidance, "*customer*" for CDD purposes was both the direct customer (which for industry purposes, is usually the buyer's broker) and the "ultimate customer" (i.e. the "end" buyer). However, revisions to the Guidance have since removed the notion of "ultimate customer". In some cases, and with reference to the examples of multi-party transactions given in the Guidance, this amendment may serve to streamline the CDD process.

The identify of a person "behind" a transaction however remains relevant and important. AMPs have obligations under the Proceeds of Crime Act 2002 ("**POCA**") and UK Sanctions Regime to ensure that they are not dealing with or transacting with any sanctioned person. AMPs may therefore need to conduct further checks which may involve the AMP identifying and verifying the identity of the person "behind" a transaction to ensure compliance. Careful consideration must also be given to the definition of "beneficial owner", under the MLRs, which can include, "*the individual … on whose behalf a transaction is being conducted*". Reg 28(4) of the MLRs requires AMLs to "*identify the beneficial owner*" and "*take reasonable measures to verify the identity*

of the beneficial owner so that the relevant person is satisfied that it knows who the beneficial owner is".

Updates to the proceeds of Crime Act 2002

The Economic Crime and Corporate Transparency Act 2023 ("**ECCTA**") came into force on 26 October 2023 with the objective of taking forward the government's focus on combatting economic crime and increasing corporate transparency. In line with this, the ECCTA brought about important amendments to POCA, many of which became effective on 15 January 2024. Of key significance for AMPs are the provisions relating to *mixed property transactions and, customer information sharing*.

Mixed Property Transactions

In accordance with section 183 ECCTA, where a business in the regulated sector (i.e., an AMP) converts, transfers or removes criminal property in the course of business on behalf of a client into an account and that business knows or suspects that some of the amount in the account is criminal property, but cannot identify which part, the business can deal with the property in the account, so long as the value of the funds in the account does not reduce to less than the value of the criminal property.

Previously, where a business received funds which were believed to be criminal property into an account, the entire account was deemed to be "tainted" and could not be dealt with in any way, without permission being received from the National Crime Agency ("**NCA**") in the form of a DAML. The amendments brought in by the ECCTA are therefore particularly helpful where an AMP operates a mixed account. Going forward, where funds are received which are suspected to represent criminal property, the AMP may continue to deal with the account (e.g., pay wages and overhead costs), so long as the balance of the account does not fall below the value of the suspected criminal property.

Customer Information Sharing

Historically, businesses in the regulated sector (including AMPs) have been constrained in their ability to share information regarding customers. The amendments to POCA, contained in section 188 of the ECCTA, are designed to make it easier for relevant businesses to be able to share customer information with each other for the purposes of preventing, investigating and detecting economic crime, by removing civil liability for breaches of confidentiality where information is shared for such purposes.

In accordance with section 188 ECCTA, businesses in the regulated sector may share information where the entity sharing the information ("A"), is satisfied that the disclosure of the information to B would assist B in carrying out the relevant functions of B, for example the prevention or detection of economic crime. Note, information subject to legal privilege cannot be shared, however, in all other circumstances, A may share the information with B, without breach of confidentiality or civil liability on the part of A.

In order for the provisions of section 188 to apply, either the request condition or the warning condition must be met:

1) Request Condition: where disclosure is made by A in response to a request by B and, at the time the request is made, B has reason to believe A holds information about a customer of A which would / might assist B in carrying out the relevant functions of B; or

2) Warning Condition: due to risks of economic crime, A has decided to take safeguarding action against the relevant customer.

Within the Art Market, the provisions of section 188 ECCTA should serve as particularly useful for the identification and communication of "red flag" clients who are known across the market.

Updates to the List of High-Risk Jurisdictions

In accordance with the provisions of the MLRs, regulated businesses are required to undertake enhanced due diligence ("**EDD**") measures and enhanced ongoing monitoring in any business relationship or transaction with a person or entity established in a "*high risk third country*".

The Money Laundering and Terrorist Financing (High Risk Countries) (Amendment) Regulations 2024 came into force on 23 January 2024 (the "**2024 Regulations**"). Prior to the publication of the 2024 Regulations, the list of high risk third countries was set out in Schedule 3ZA of the MLRs. The 2024 Regulations have however, deleted and replaced Schedule 3ZA by redefining high risk third countries as those countries identified by the FATF on either of the lists it publishes from time to time, known as the "black list" and the "grey list", available here:

"Black and grey" lists (fatf-gafi.org)

The 2024 Regulations are intended to streamline updates to the list of high-risk jurisdictions in respect of which EDD must be conducted by aligning the UK list with the FATF lists.

AMPs, as regulated businesses, must take note of the FATF lists, and ensure that policies and procedures are updated to reflect the revised list. Crucially, EDD and enhanced ongoing monitoring must be applied to all customers, new and existing, established in any of the high-risk jurisdictions, as identified by the FATF lists.

What to do next

In line with the updates noted above and the Government's renewed focus on fighting economic crime particularly within what it deems high risk sectors, AMPs need to be more vigilant than ever in ensuring that they have in place policies and procedures which comply with the relevant regulatory regime.

We have set out below four key takeaways for AMPs:

1) AMPs should review their Anti-Money Laundering polices against the new BAMF Guidance and update those policies where necessary;
2) AMPs should ensure they remain up to date on legislative and policy amendments as they are released, including the FATF lists and NCA / BAMF bulletins and guidance;
3) AMPs should be prepared in the event of an inspection from HMRC and take note of the need to demonstrate compliance with applicable legislation and show the existence of robust systems; and
4) AMPs should be aware of the obligation to disclose and the new rules on information sharing and mixed property transactions.

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France's mixed canvas: the country's incomplete efforts towards the restitution of looted art

On 22 July 2023, eighty-two years after the entry into force of the "Aryanisation" law of 22 July 1941,[1] France adopted a landmark law that aims to significantly facilitate the restitution of artworks stolen between 1933 and 1945 and integrated into the French national collection.

France's dual regime for restitution on Nazi-looted art

The legal framework regarding looted artworks in France has long been unsatisfactory, at best. French law traditionally distinguishes between cultural assets that left French soil, were found in Germany and were subsequently sent back to France immediately after the Second World War ("MNRs"),[2] and artwork that belonged to an owner who was dispossessed, which was integrated, possibly in good faith, into French public collections, without acknowledgment of prior dispossession.

- MNRs are currently entrusted to the care of French national museums and legally overseen by the French Ministry of Foreign Affairs. They are not considered part of the State's heritage and are catalogued in special inventories, pending potential restitution to their owners, at any time; no statute of limitation is imposed on such restitution claims.
- Artwork that has been integrated into the State's heritage and the French public domain, on the other hand, cannot be claimed as easily, as they are subject to the principle of "inalienability" of the public domain, pursuant to Article L. 3111-1 of the French General Code on the Property of Public Persons and Article L. 451-5 of the French Heritage Code. This fundamental principle of French law, while safeguarding the French public domain, has inadvertently entangled looted artworks in a legal limbo, preventing their rightful return to the heirs of their original owners.

Historically, as a result of the principle of inalienability of the public domain, any cultural asset that had entered French public collections could only be restituted through the adoption of a special law, promulgated on a case-by-case basis. By way of example, the law of 21 February 2022[3] authorized the restitution of fifteen artworks from French public collections, looted prior to and during the Second World War: an unsatisfactory solution to a global issue, when it is estimated that at least 100,000 artworks were looted during this period.

Degenerate art stolen by Nazis in the Jeu de Paume Museum in Paris, during the Second World War

The Law of 22 July 2023 henceforth seeks to offer a more comprehensive solution to the issue, abandoning the need to pass a specific law for every claimed work of art.

What does the new Law of 22 July 2023 change?

Law No. 2023-650 of 22 July 2023 addresses the restitution of cultural assets that were looted in the context of antisemitic persecutions, carried out between 1933 and 1945. This legislation, unanimously adopted by the French National Assembly and the French Senate and promulgated

[1] Under which the Vichy regime put in place a specific policy of persecution and spoliation of Jewish people in France that effectively permitted the plunder of their belongings.
[2] It should be noted that the French authorities returned to France all property found in Germany that had left France during the Occupation, regardless of how it had left the country: property sold in France during the Occupation by owners who were not persecuted was also recovered and returned to France.
[3] Law No. 2022-218 of 21 February 2022.

by the President, amends the French Heritage Code to facilitate the return of such items to their rightful owners or heirs. Specifically, it introduces a provision allowing for the declassification of looted cultural goods from French public collections, enabling their restitution. This process constitutes an exception to the rule, deviating from the principle of inalienability that typically applies to French public collection assets.

Scope. The Law of 22 July 2023 is designed to address the restitution of artworks looted during the period of antisemitic persecutions between 30 January 1933 and 8 May 1945, and applies to artworks currently held in French collections, including those that were looted outside of France. The legislation extends its reach to include artworks donated or bequeathed to museums under the "Musée de France" label, ensuring that French private collections are also subject to restitution and compensation mechanisms.

Mechanism. The Law of 22 July 2023 tasks a pre-existing specialized administrative commission, the Commission for the Compensation of Victims of Antisemitic Spoliation during the Occupation (CIVS), placed under the auspices of the French Prime Minister, with evaluating restitution claims. This commission's advisory role is pivotal, ensuring that each case of restitution is underpinned by an independent and rigorous assessment of the circumstances of the relevant looting.

Alternative reparation. The legislation provides innovation insofar as it also allows for the negotiation of financial compensation, or other forms of reparation, when physical restitution is not the most adapted solution.

The Law of 22 July 2023 provides that it is applicable to ongoing restitution claims from the date of its publication.

The mixed impact of the Law of 22 July 2023

In many ways, the Law of 22 July 2023 is a significant step towards improving restitution of looted artworks to victims of antisemitism. Not only does it considerably simplify the procedure for claiming a looted work of art, but it also highlights the need for French public and private collections, as well as art dealers, auction houses and experts, to conduct thorough provenance research and due diligence to prevent the circulation of looted art.

However, the Law of 22 July 2023 does face limitations, particularly concerning artworks located outside of France. The law's reach is inherently confined to national boundaries, leaving the issue of looted artworks in foreign museums or private collections unresolved. This challenge is compounded by the lack of any overarching binding international legal framework. Despite notable public declarations of intent,[4] only five countries have established national commissions to examine restitution claims.[5]

Moreover, the European Union has not implemented specific instruments for the restitution of artworks looted during Nazi-era antisemitic persecutions, treating restitution as a matter falling within the jurisdiction of Member States and their domestic law.[6] This situation leads to significant legal challenges, especially where the circulation of a cultural object across territorial borders introduces conflicts of law and/or conflicts of jurisdiction complexities. Typically, international private law would defer to the law of the country where the artwork is currently located (*lex rei sitae*), potentially overlooking the law of the artwork's origin (*lex originis*), when the latter could potentially provide a more adequate basis for restitution claims. The current legal landscape suggests that, while France's new law is a step in the right direction, achieving global restitution for Nazi-looted artwork will require international cooperation and a more unified and harmonized cross-border legal approach.

In addition, beyond its limited territorial scope, the Law of 22 July 2023 evidently does not address artworks falling outside its ambit, and in particular, the restitution of artworks located in the former colonies of Western empires. The French government has since passed another framework restitution law, addressing the restitution of human remains belonging to French public collections.[7] The French government also plans on passing a new law stipulating guidelines allowing the deaccessioning of art taken from Africa, and other regions, during the colonial era. However, a first draft bill of this new law, submitted to the French Senate on 12 October 2021, has been at a standstill, since 12 July 2022, before the French National Assembly's Commission of Cultural Affairs and Education, with no foreseeable evolution in sight.

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[4] Such as the Washington Conference Principles on Nazi-Confiscated Art (1998), the Vilnius International Forum on Holocaust Era Looted Cultural Assets Declaration (2000) and the Terezin Declaration on Holocaust Era Assets and Related Issues (2009).

[5] Germany, Austria, the Netherlands and the United Kingdom.

[6] The European Parliament adopted a resolution on 17 January 2019 on cross-border restitution claims of works of art and cultural goods looted in armed conflicts and wars, and called on the European Commission to protect, support and encourage restitution.

[7] Law No. 2023-1251 of 26 December 2023.

Thus, in the interim, specific laws must still be enacted, on an exceptional and case-by-case basis, in order to restitute artworks without falling foul of the principle of inalienability of French public collections. For example, as an exception to this principle, the Law of 24 December 2020[8] provided for the removal from national collections of twenty-six artworks from Abomey and El Hadj Omar Tall's sabre, and their restitution to the Republic of Benin and the Republic of Senegal respectively.

While France may have come to terms with its role in the perpetuation of antisemitic acts during the Second World War, thus accepting its responsibility in the spoliation of Jewish victims of expropriation and the need to restitute looted artworks from that period, its colonial history remains a sensitive subject that may potentially be the backdrop for a heated and protracted debate in the French Parliament.

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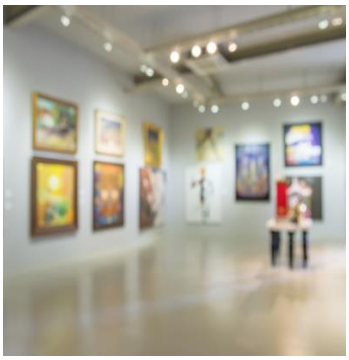
[8] Law No. 2020-1673 of 24 December 2020.

The cultural heritage sector's originality question – Impact of *THJ v Sheridan*



Does a gallery or museum have the right to claim copyright protection over and monetise access to its digital reproductions of artwork when the artwork itself is out of copyright?

This common practice and hotly-debated issue in the UK art and cultural heritage sector has been brought into sharp focus by a recent ruling of the Court of Appeal of England and Wales in the case of *THJ v Sheridan [2023] EWCA Civ 1354*. The case deals with copyright protection, specifically the complex nuances of what qualifies an artistic work as "original" under UK copyright law such that it enjoys copyright protection. Although the case does not address photographic reproductions of artwork specifically, the judgment contains important commentary on the question of originality more generally which applies equally to the art world.

The decision

THJ v Sheridan concerned the question of whether copyright subsists in certain graphic user interfaces ("**GUIs**") in the form of "risk and price charts" ("**R&P Charts**") produced using a software program. The judgment reiterated and clarified the objective legal test of originality for determining whether copyright subsists in artistic works.

The claimants contended that the R&P Charts qualified as artistic works under Section 4(1)(a) of the Copyright, Designs and Patents Act 1988 ("**CDPA**"). In order to assess whether copyright subsists in these R&P Charts, the Court of Appeal had to determine whether they were "original" in accordance with Section 1(1)(a) of the CDPA which provides that an artistic work must be "original" in order for copyright to subsist in it.

Historically, English law had a low originality threshold. A work was considered original if it was the result of an author's deployment of labour, skill and judgement. Thus, copyright would subsist in a work if the author of such work had exercised some degree of "skill and labour" to create it. However, the Court of Justice of the European Union ("**CJEU**"), in its decision in *Infopaq International A/s v Danske Dagblades Forening* and a series of subsequent judgments expanded the "skill and labour" test by introducing a more stringent requirement that an "author's own intellectual creation" should be an additional criterion to gauge originality of an artistic work. Thus, according to the current elevated test, in order to qualify as "original", a work must be the outcome of the author's exercise of "creative freedom" and contain the author's "personal touch".

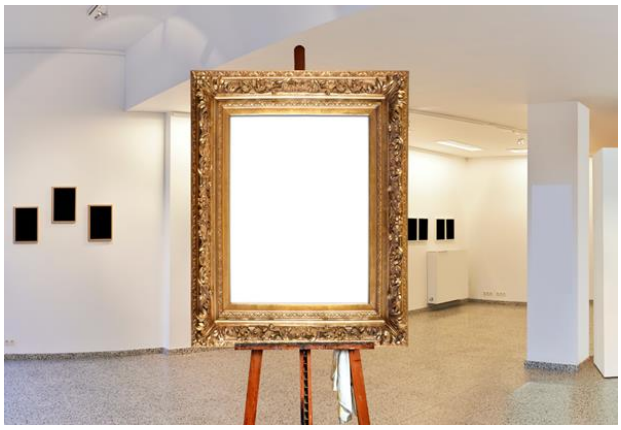
In *THJ v Sheridan*, Lord Justice Arnold, who gave the leading judgment, restated the CJEU's higher threshold of originality and held:

"*The Court of Justice has elaborated upon the requirement that the work be its author's own intellectual creation in a number of subsequent judgments. What is required is that the author was able to express their creative abilities in the production of the work by making free and creative choices so as to stamp the work created with their personal touch …* ***This criterion is not satisfied where the content of the work is dictated by technical considerations, rules or other constraints which leave no room for creative freedom.***" [Emphasis added]

The Court of Appeal agreed with the defendants that the first-instance judge had applied the outdated "skill and labour" test, instead of the elevated "author's own intellectual creation" test. Nevertheless, the Court of Appeal in reassessing the originality of the R&P Charts and applying the correct legal test continued to hold, as the first instance judge had done despite applying the wrong test, that the R&P Charts were original. This was because the claimant had made creative choices in laying out the various components of the R&P Charts and was responsible for the overall design and visual appearance of the charts. It was not contended by the defendants that the configuration of the various components was dictated by technical considerations. Lord Justice Arnold further reiterated that the originality test was an objective one consistent with Section 4(1)(a) of the CDPA that sets out that graphic works (such as GUIs) qualify as artistic works "irrespective of artistic quality". Thus,

it was not a requirement that the R&P Charts should be of any artistic merit.

Impact on the UK art and cultural sector



The judgment has significant relevance in the UK art and cultural heritage sector as it has challenged and brought into question the validity of the legal basis on which UK cultural heritage institutions (such as museums, galleries, archives and libraries) monetise digital reproductions of artworks that are out of copyright, by claiming that copyright subsists in the digital reproductions and charging fees for their use and reproduction. Traditionally, such institutions had relied on the low threshold of originality based on the old "skill and labour" test according to which such images enjoyed copyright protection if the photographer deployed a certain degree of skill, labour and effort in creating the images, even if the underlying artwork was in the public domain.

There is no question post *THJ v Sheridan* that in order for copyright to subsist in such digital reproductions they must now satisfy the elevated originality threshold of the "author's own intellectual creation". However, this was the case even before the judgment in *THJ v Sheridan*. The *Infopaq* decision came into force prior to Brexit, and it therefore forms part of the body of UK copyright law. In order for copyright to subsist, this would require the photographer to exercise free and creative choices and leave their personal intellectual imprint in creating the digital images, as opposed to being restricted by technical considerations and constraints. Thus, whether digital reproductions of museum collections will be copyright protected would depend on the process of creating the digital reproductions: did it involve free decision-making and creativity or was it was purely dictated by technical considerations of producing the most realistic, high quality and accurate reproductions.

Given the standard set out in *THJ v Sheridan*, it can be argued that a digital reproduction of a public domain artwork created specifically for a museum's purposes, lacks the necessary exercise of intellectual creation and creative decision making and would not qualify as an original work. Further, the creation of these images arguably would involve conforming to certain rules and other constraints to ensure the production of high quality and accurate images for the museum's commercial purposes. For example, the images would have to be captioned, catalogued and colour corrected in a standardised and technical manner which might thwart the creative freedom and personal intellectual markings of the photographer. In such a process, there might be limited scope for the photographer to exercise any creative choices if the purpose was merely to make a faithful digital record of an existing artwork. Thus, such digital images would fail to meet the originality threshold and would be free for use by the public as the museums would have no right to assert that copyright subsists in them.

However, commentators who have criticised museums and galleries for claiming that copyright subsists in digital reproductions may have focussed too heavily on Arnold LJ's comment that the originality criterion is not satisfied where the content of the work is dictated by technical considerations, rules or other constraints which leave no room for creative freedom. The judgment also commented that even a simple photograph could satisfy the objective originality test, and that a low degree of visual creativity would not necessarily mean the absence of originality, though it may warrant a low level of copyright protection. In *C-145/10 Eva-Maria Painer v Standard VerlagsGmbH and Others (Third Chamber) [2011] ECR I-12533*, which was cited favourably in *THJ v Sheridan*, the CJEU held that even a simple portrait photograph may satisfy the originality test in an appropriate case, as long as the photographer exercised some degree of creativity and personal vision in setting up and capturing the photograph, irrespective of its artistic quality. The CJEU observed:

"*Even though the essential object of such a photo is already established in the person of the figure portrayed, a photographer still enjoys sufficient formative freedom. The photographer can determine, among other things, the angle, the position and the facial expression of the person portrayed, the background, the sharpness, and the light/lighting. To put it vividly, the crucial factor is that a photographer 'leaves his mark' on a photo.*"

Thus, it could also be argued that cultural heritage organisations may have a narrow scope of protection in relation to certain digital images where the photographer has exerted an adequate degree of creativity and personal touch in creating them. The

picture is not so "black and white" as some critics of museums and galleries have made out.

It is also important to note, that the CJEU has received several referrals asking it to clarify the "author's own intellectual creation" criteria for determining the originality of works and the standard may evolve further, at least at EU level.

Considerations for UK museums, art galleries and cultural heritage organisations

The elevated originality standard stemming from the harmonisation of EU and UK copyright law in the absence of any statutory reform in the UK should prompt cultural heritage institutions to strategise and rethink their policies on how to best protect and commercialise their assets. While there is uncertainty around whether institutions may be able to continue claiming copyright protection over assets such as digitised images of their out-of-copyright collections, they may very well be able to rely on alternative legal means such as contract law to regulate access to these images and charge fees for their circulation and use. Some institutions, however, may decide to tread differently by making these images readily available to the public. They may do this either for free or by charging nominal service-based fees with the goals of promoting inclusivity, widening access to art and building public goodwill, while diverting their investment to other more profitable revenue streams. It will be interesting to see in which way the cultural heritage sector chooses to respond and whether the courts have an opportunity to provide any commentary on what is meant by an "author's own intellectual creation" in the context of the art world specifically.

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Art – is it worth considering structuring?

Should I hold an art collection in a trust? In a company? In my own name? Does it make a difference if it's hanging on my wall? Art and tax are not words that frequently come up in the same sentence, but they are worth considering together. This article discusses certain options for structuring art collections and their benefits and pitfalls from a UK tax perspective.

The questions above depend on the individual themselves ("**X**") – and not only their preferences and interest (if any) in trust or company structuring but also their personal circumstances. This article assumes that X is UK resident and non-UK domiciled or, in the alternative, UK resident and deemed domiciled in the UK where these types of questions often arise.

To provide some brief context, persons who are UK resident but do not have a domicile of origin in the UK (broadly meaning they were not born to UK parents) or a domicile of choice in the UK (broadly meaning they are not present in the UK with the intention to remain here permanently or indefinitely – in other words, they do not intend to end their days in the UK) will be non-UK domiciled. However, once an individual has been resident in the UK for 15 out of the previous 20 UK tax years they will be deemed domiciled in the UK. This is regardless of whether they are still non-UK domiciled or not.

Trust ownership

One option is to hold art in a trust structure. This could be, for instance, a non-UK discretionary trust settled by X or a non-UK discretionary trust settled by another where X is a beneficiary. The art may be held by the trustees of the trust, or by an underlying company to the trust.

The advantage of using a trust to hold art is the inheritance tax saving. Holding art in trust means it can fall outside of X's estate for inheritance tax purposes. Provided the trust is settled by X when they are non-UK domiciled and the art is kept outside of the UK, no inheritance tax charges will arise for X or for the trustees of the trust itself.

However, if the art will be enjoyed by X because it hangs on their wall in the UK (for example) and X is a beneficiary and the settlor of the trust or X added property to the trust which was settled by another then it is preferable from an inheritance tax perspective for the art to be held by a non-UK company owned by the trust (although bearing in mind the other UK tax issues associated with company ownership referred to below). This is to ensure no inheritance tax charges arise for X under the "gift with reservation of benefit" rules.

Another issue to bear in mind is whether the trust already holds other assets or has non-UK source income and/or gains that have arisen to the trust in the past.

If the trust contains non-UK source income and/or gains that have not been paid out of the trust or used to meet expenses (for example) in the UK tax year that they arise, that income and/or gains will be available to match against any benefit received from the trust. If X hangs the art on the wall of their UK

home then they have received a benefit from the trust. The benefit would be matched, and an income or capital gains tax charge could arise for X. The amount of the benefit (and so the tax charge) would be based on HMRC's official rate of interest (currently 2.25%) multiplied by the acquisition cost of the art or, if it was not acquired in an arm's length transaction, its market value at the date of acquisition plus any expenditure incurred subsequently for the purpose of enhancing its value less any repair, insurance, storage costs or rent paid by X for use of the art.

However, if the trust holds no other assets and is "dry", in other words no non-UK source income or gains arise to the trust which are available to be matched, then it may be an efficient way of holding art and enjoying it in the UK. No UK tax would be due unless and until there were funds available to be matched.

An alternative is for X to pay rent to the trustees of the trust for use of the art in the UK. However, this would mean adding UK source income to the trust which the trustees would have to report to HMRC and tax would be payable.

As a further point, if the art is sold whilst it is held by the trust then any gain that arises on the sale will be added to the pool of other gains (if any) within the trust. Those gains may be available to be matched against any prior untaxed benefits (where there were no income or gains in the trust until the sale of the art) and any future benefits that UK resident beneficiaries receive from the trust, resulting in a UK tax charge for those beneficiaries.

Company ownership

Another option is to hold an art collection through a company. This provides some protection from inheritance tax if the value of the shares in the company is less than the value of the art that it holds. The value of the shares in the company would be within X's estate for inheritance tax purposes (rather than the art itself). Taking this a step further, if the company is non-UK incorporated and X is non-UK domiciled and not deemed domiciled then X would not be subject to inheritance tax on the shares in the company (or the art it holds).

X needs to consider how the company is funded. If non-UK source income or gains are added to the company and used to purchase art and that art is brought to the UK, this can result in income and/or capital gains tax liabilities for X when the art is imported. This is the case if X is unable to or fails to claim the benefit of the "remittance basis" of taxation. The remittance basis can only be claimed by individuals who are non-UK domiciled and not yet deemed domiciled in the UK, and in essence provides that X will be subject to UK tax on non-UK source income or gains only if they (or certain persons connected to them) bring these to the UK.

The other consideration is "benefit in kind" charges, which can be punitive. If X is a director of the company (or the other directors of the company are accustomed to acting in accordance with X's wishes, so that X is a "shadow" director) and X benefits from the art as it hangs on their wall for example then these charges can arise. The charge is based on the cost to the company. One solution is for X to pay rent to the company for use of the art in order to avoid paying the benefit in kind charge, but again this can give rise to UK source income for the company which would be subject to tax.

Where the art is later sold by the company in the UK and a gain arises, this gain would be subject to tax on X. However, if the art was taken out of the UK and then sold, a UK tax charge would only arise if X was deemed domiciled in the UK at the time or did not claim the benefit of the remittance basis or if X did claim the benefit of the remittance basis and either X or certain persons connected to X brought the proceeds back to the UK. Export restrictions would also need to be considered in that context.

Personal ownership

A third option is to hold the art collection personally. The first consideration is how the purchase of the art is funded. If the art was already purchased by X using non-UK income or gains outside of the UK and is subsequently brought to (i.e. remitted to) the UK, this can give rise to income or capital gains tax on the original funds used to purchase the art if those funds have not already been subject to UK tax or are not "clean capital". Clean capital includes inherited funds and income and gains that arose before X became UK resident.

There are exemptions, however, where no remittance will occur. The exemptions include circumstances where the art is available for public access whilst it is in the UK through a museum, gallery or similar institution or the art is brought to the UK for repair or restoration. There is also an exemption for art that is brought into, received or used in the UK for 275 or fewer days. However, such exemptions are less useful where X wishes to enjoy the art themselves.

If, however, art is purchased in the UK using UK source income or gains (or clean capital) then no further UK tax charge on the purchase arises.

If a single work of art is sold in the UK and is worth more than £6,000, any gain in value would be liable to capital gains tax. However, if the art was taken out of and sold outside of the UK, a capital gains tax liability would only arise if X was deemed domiciled in the UK (or not claiming the benefit of the remittance basis of taxation at the time) or the proceeds of sale were later brought back to the UK.

If the art remains in X's estate on death and is located in the UK (or X is deemed domiciled), it will be subject to inheritance tax. However, it is possible to insure against that liability. There are also concessions available for inheritance tax on certain works of art, provided the art is pre-eminent and public access is given, maintained and preserved. The art must also be kept in the UK, and the concession does not remove the inheritance tax but defers it. As a result, if and when the art is sold the inheritance tax becomes payable.

Conclusion

To conclude, whether it is worth structuring art collections through a company, trust or combination of the two will depend on the particular circumstances of the individual, whether they have pre-existing trusts (in which case a trust structure may be more viable in terms of cost) and the value and extent of the art collection amongst other considerations. In many cases it may be simpler for X to hold art in their personal capacity, and a further factor is the extent to which UK taxes (or a particular UK tax, such as inheritance tax) are of concern to the individual.

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