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COMMENT

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DEVISING AN ARTFUL TAX: AN APPRAISAL  
OF PAYMENT-IN-KIND INCOME TAXES IN  
MEXICO AND THE UNITED KINGDOM

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#### INTRODUCTION<sup>1</sup>

According to popular accounts, in 1957 David Alfaro Siqueiros marched into Hugo B. Margáin's office with a radical and risky proposal.<sup>2</sup> There, the

<sup>1</sup> To facilitate the use of Spanish-language sources, I have translated several quoted passages into English throughout this Comment. In these instances, I have attempted to preserve the original meaning as accurately as possible.

<sup>2</sup> See Edgardo Ganado Kim, *La Colección Pago en Especie, Una Historia por Completar* (detailing how Siqueiros arrived at the interview with Margáin in "the combative character that distinguished him"), in COLECCIÓN PAGO EN ESPECIE DE LA SECRETARÍA DE HACIENDA Y CRÉDITO PÚBLICO 1997–2002, at i (2004); Ana Garduño, *Pago en Especie: A 55 Años de un Convenio Patrimonializador*, 34 ANALES DEL INSTITUTO DE INVESTIGACIONES ESTÉTICAS 231, 232 (2012), <http://www.redalyc.org/>

famous muralist bluntly told the new Director of Income Tax that the recent income tax reforms were unduly burdening Mexico's artists because they "did not know about accounting or tax laws"<sup>3</sup> and had no money with which to pay their obligations.<sup>4</sup> "The only thing we have are paintings," Siqueiros insisted.<sup>5</sup> However, rather than seek a complete tax exemption for artists, he told Margáin that artists could instead pay taxes with their artwork.<sup>6</sup> Because their art was valuable, Mexico could amass an enviable collection.<sup>7</sup> Tasked with ensuring the success of the new tax system,<sup>8</sup> perhaps Margáin was inclined to be creative, or perhaps he was an art aficionado. Regardless of his motives, Margáin replied, "It doesn't seem like a bad idea."<sup>9</sup> Under Margáin's leadership, the Mexican Ministry of Finance and Public Credit accepted Siqueiros' proposal and launched a program called *Pago en Especie* (Payment in Kind) in November 1957, when it collected its first income tax payment in art.<sup>10</sup>

Now in effect for almost sixty years, *Pago en Especie* allows Mexican artists to satisfy their annual income taxes by giving the government a certain number of their paintings, sculptures, drawings, photographs, or other visual works each year.<sup>11</sup> Although no cash payment occurs, the government sees tremendous value in these acquisitions.<sup>12</sup> Endowed each year with more artwork, the government now boasts the world's premier collection of Mexican contemporary art, with

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articulo.oa?id=36923225008 [https://perma.cc/SMS8-FG7M] (narrating the colorful version of Siqueiros' visit that is frequently recounted in the Mexican Ministry of Finance and Public Credit's catalogues).

<sup>3</sup> Garduño, *supra* note 2, at 232.

<sup>4</sup> See Ganado Kim, *supra* note 2, at i (recounting how Siqueiros justified his proposal).

<sup>5</sup> Garduño, *supra* note 2, at 232.

<sup>6</sup> *Id.*

<sup>7</sup> Ganado Kim, *supra* note 2, at i.

<sup>8</sup> See María de los Ángeles Sobrino Figueroa, *Diego Rivera en el Acervo Patrimonial de la Secretaría de Hacienda y Crédito Público* (describing Margáin's responsibilities in implementing the new income tax system, which included "finding mechanisms to simplify the payment of taxes"), in DIEGO RIVERA (1886–1957): CATÁLOGO HOMENAJE 31, 31 (2007).

<sup>9</sup> *Artists Pay Tax Bills in Mexico with Art*, NEWSELA (Aug. 4, 2014), https://newsela.com/articles/mexicanartists-taxtime/id/4645 [https://perma.cc/248W-VQXX].

<sup>10</sup> See José Ramón San Cristóbal Larrea, *Historia de Una Colección: Programa Pago en Especie*, MEXICANÍSIMO, no. 40, at 34, 37–38, http://www.museocjv.com/pagoenespecie.pdf [https://perma.cc/E4HQ-2EK9] (describing how Margáin oversaw the first collection of art from 1957 to 1958); Sobrino Figueroa, *supra* note 8, at 31 (detailing how *Pago en Especie* began operating in November of 1957).

<sup>11</sup> See Merry MacMasters, *Pago en Especie Cumple Medio Siglo y Acumula Más de 5 Mil Obras*, LA JORNADA (Dec. 5, 2007), http://www.jornada.unam.mx/2007/12/05/index.php?section=cultura&article=ao4n1cul [https://perma.cc/X4XX-98KF] (discussing the various types of art submitted to the *Pago en Especie* collection).

<sup>12</sup> See Decreto que Otorga Facilidades para el Pago de los Impuestos Sobre la Renta y al Valor Agregado y Condona Parcialmente el Primero de Ellos, que Causen las Personas Dedicadas a las Artes Plásticas, con Obras de Su Producción, y que Facilita el Pago de los Impuestos por la Enajenación de Obras Artísticas y Antigüedades Propiedad de Particulares, Diario Oficial de la Federación [DOF], 31-10-1994 (Mex.) [hereinafter Decree of 1994], http://www.sat.gob.mx/fichas\_tematicas/pago\_especie/Paginas/default.aspx [https://perma.cc/98QG-9GRD] (explaining that allowing artists to submit art instead of paying federal income taxes will augment Mexico's cultural heritage).

close to 7000 works.<sup>13</sup> Artists also view the scheme favorably.<sup>14</sup> Relieved of paperwork, audits, and counting pesos, an artist can devote himself completely to his creativity and take pride in knowing that the work he submits on tax day will become part of a national repository.<sup>15</sup>

While no other country has gone as far as Mexico in adopting a payment-in-kind tax program for art, in 2012 the United Kingdom passed legislation authorizing the Cultural Gifts Scheme (CGS), which allows *all* taxpayers—not just artists—to donate a preeminent object to a qualifying institution in the United Kingdom.<sup>16</sup> As in Mexico, individual taxpayers and the government both reap significant benefits from this program. For a taxpayer, the tax reduction earned for donating a preeminent object may significantly decrease the income taxes owed.<sup>17</sup> For the United Kingdom, CGS ensures that important cultural and artistic works remain in the country and continue to enrich the nation's cultural landscape.<sup>18</sup>

As *Pago en Especie* and CGS have gained more attention, there have been rumblings that the United States should consider implementing a similar payment-in-kind income tax program for contemporary artwork and other forms of cultural property.<sup>19</sup> Simplifying tax payments, accommodating

<sup>13</sup> Eva Hershaw, *In Mexico, Artists Can Pay Taxes with Artwork*, ATLANTIC (Apr. 11, 2014), <http://www.theatlantic.com/international/archive/2014/04/in-mexico-artists-can-pay-taxes-with-artwork/360519> [https://perma.cc/N7G6-T7S5].

<sup>14</sup> See Tim Johnson, *When Mexico's Tax Time Comes, Artists Get Busy with the Brushes*, MCCLATCHY DC (July 15, 2014), <http://www.mcclatchydc.com/news/nation-world/world/latin-america/article24770509.html> [https://perma.cc/D6YA-EYK4] (interviewing artists who support *Pago en Especie* and speaking with curators who believe that *Pago en Especie* has “generated good will among artists”).

<sup>15</sup> *Id.*

<sup>16</sup> Finance Act 2012, c. 14, sch. 14 (Eng.), [http://www.legislation.gov.uk/ukpga/2012/14/pdfs/ukpga\\_20120014\\_en.pdf](http://www.legislation.gov.uk/ukpga/2012/14/pdfs/ukpga_20120014_en.pdf) [https://perma.cc/H373-ELTP].

<sup>17</sup> ARTS COUNCIL ENG., ACCEPTANCE IN LIEU: REPORT 2013, at 4 (2013) [hereinafter AIL: REPORT 2013], [http://www.artscouncil.org.uk/media/uploads/pdf/Acceptance\\_in\\_Lieu\\_publication\\_Nov13.pdf](http://www.artscouncil.org.uk/media/uploads/pdf/Acceptance_in_Lieu_publication_Nov13.pdf) [https://perma.cc/3QBX-VPAV].

<sup>18</sup> See ARTS COUNCIL ENG., CULTURAL GIFTS SCHEME & ACCEPTANCE IN LIEU: REPORT 2014, at 4 (2014) [hereinafter CGS & AIL: REPORT 2014], [http://www.artscouncil.org.uk/media/uploads/Cultural\\_Gifts\\_Scheme\\_and\\_Acceptance\\_in\\_Lieu\\_publication\\_Nov14.pdf](http://www.artscouncil.org.uk/media/uploads/Cultural_Gifts_Scheme_and_Acceptance_in_Lieu_publication_Nov14.pdf) [https://perma.cc/ATA3-WHX4] (noting that these donations will “augment museums and collections” and “delight and inspire the many millions who visit [them]”).

<sup>19</sup> Compare *In Mexico, Artists Pay Taxes with Paintings*, TAKEAWAY (Apr. 14, 2010), <http://www.thetakeaway.org/story/35475-mexico-artists-can-offer-government-talent-taxes> [https://perma.cc/ZR85-WD8U] (interviewing a museum director who has called for the United States to adopt an income tax scheme like *Pago en Especie*), and Robert W. Wood, *Paying Tax With Art is Legal in UK & Mexico, Why Not in US?*, FORBES (Sept. 10, 2014, 11:27 PM), <http://www.forbes.com/sites/robertwood/2014/09/10/paying-tax-with-art-is-legal-in-uk-mexico-why-not-in-us> [https://perma.cc/ZLR6-9E6A] (highlighting the benefits of payment-in-kind systems, including the creation of good will within the art community, the development of a national collection, and the decoration of public spaces), with Rob Maguire, *Should Artists Be Able to Pay Taxes with Artwork?*, ART THREAT (Apr. 11, 2014), <http://artthreat.net/2014/04/mexico-taxes-artwork> [https://perma.cc/52US-T3QD] (“Any move

artists' needs, accumulating a national collection, and promoting tourism are common justifications for adopting such programs.<sup>20</sup> However, while *Pago en Especie* and CGS initially appear attractive to artists and art lovers alike, an in-depth examination of each reveals numerous administrative, fiscal, and precedential shortcomings that could undermine—rather than enhance—a larger income tax system.

This Comment seeks to explore the issues surrounding payment-in-kind income tax schemes as they relate to art, art owners, and artists. Part I provides a comprehensive history of *Pago en Especie* and outlines how this annual collection of contemporary art occurs today. It also reviews common justifications for the program to assess how it has garnered such widespread support throughout Mexico. Part II examines the origins of CGS, explains the application process, and surveys the first items collected in exchange for a tax reduction. Finally, it evaluates the dominant explanations for why the United Kingdom adopted the new scheme. Part III then turns to the United States to contrast how the federal income tax system treats art, focusing on deductions for charitable donations and the taxation of artists.

With that background, Part IV identifies and compares the policy weaknesses inherent in *Pago en Especie* and CGS and contemplates the dangers of adopting a similar payment-in-kind program in the United States. Ultimately, Part IV contends that the United States should not adopt *Pago en Especie*, CGS, or any other payment-in-kind tax system because to do so would (1) forfeit cash revenue in a direct and selective manner; (2) pledge public funds to the future care of the collected art; (3) give public museums an advantage over private museums; (4) force the Internal Revenue Service (IRS) to make subjective determinations about what kind of art to accept; (5) set a precedent for others to demand payment-in-kind options; and (6) imperil the principles of impartiality, objectivity, and precision that help sustain the income tax system.

Finally, after briefly comparing the advantages of CGS relative to *Pago en Especie*, this Comment concludes by advising the United States to avoid a payment-in-kind income tax system altogether. Although paying income taxes with art appears to accommodate the needs of artists and highlight the importance of the arts in society, the United States should reject any tax scheme that does not promote the impartial treatment of taxpayers, objective decisions from the IRS, or a precise method of calculating the income taxes owed. By continuing to accept taxes in cash and permitting certain tax deductions for art donations, the United States can avoid many of the policy

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to adopt a similar program in . . . the United States . . . would likely be fraught with controversy and neoconservative outrage.”)

<sup>20</sup> See *infra* Sections I.D, II.C.

predicaments that *Pago en Especie* and CGS confront and preserve the integrity of the income tax system.

## I. MEXICO'S *PAGO EN ESPECIE* PROGRAM

### A. *The Historical Development of Pago en Especie*

In December 1953, a series of tax reforms culminated in the *Ley del Impuesto Sobre la Renta* (Law on Income Tax), which formally levied income taxes on visual artists.<sup>21</sup> Like other self-employed professionals, artists would thereafter have to pay tax on the income earned from the sale of their work. As the Director of Income Tax, Hugo B. Margáin was responsible for implementing the new tax system and streamlining the payment process on behalf of Mexico's Ministry of Finance and Public Credit, the *Secretaría de Hacienda y Crédito Público* (SHCP).<sup>22</sup>

By 1957, however, some artists were already struggling to pay their income taxes.<sup>23</sup> The mounting pressure on artists drew the attention of several leaders in the Mexican art community, including two influential museum directors, Inés Amor<sup>24</sup> and Carmen Marín de la Barreda,<sup>25</sup> and two revered Mexican artists, David Alfaro Siqueiros and Gerardo Murillo.<sup>26</sup> For Siqueiros in particular, the worry had become personal. One of his friends had not been able to satisfy his income taxes and faced potential imprisonment.<sup>27</sup> Together, the four conceived of an innovative alternative to alleviate the burden on artists: the government should permit artists to pay their income taxes with their most valuable possessions—their artwork.<sup>28</sup>

Prevailing accounts relate that Siqueiros secured a meeting with Margáin at the SHCP offices;<sup>29</sup> there, he forcefully explained how the new income tax unduly burdened artists, who were inexperienced with accounting and the law

<sup>21</sup> See Garduño, *supra* note 2, at 231 & n.1 (recounting the manner in which artists were first incorporated into the tax system).

<sup>22</sup> See Sobrino Figueroa, *supra* note 8, at 31 (describing “the arduous task” that Margáin faced in implementing the new income tax legislation under President Adolfo Ruíz Cortínez (1952–1958)).

<sup>23</sup> See Ganado Kim, *supra* note 2, at i (acknowledging that many artists simply could not afford to pay income taxes in the 1950s).

<sup>24</sup> Inés Amor was the Director of the Galería de Arte Mexicano at the time. San Cristóbal Larrea, *supra* note 10, at 37.

<sup>25</sup> Carmen Marín de la Barreda was then the Director of the Salón de la Plástica Mexicana. *Id.*

<sup>26</sup> See *id.* (identifying the four visionaries who laid the groundwork for *Pago en Especie*).

<sup>27</sup> See Hershaw, *supra* note 13 (describing how Siqueiros sought “to keep a friend and fellow artist out of jail for tax evasion”); Johnson, *supra* note 14 (noting that Siqueiros had a friend who was threatened with “jail time for not paying taxes”).

<sup>28</sup> See San Cristóbal Larrea, *supra* note 10, at 37 (detailing how this group devised the plan for *Pago en Especie*).

<sup>29</sup> Garduño, *supra* note 2, at 232.

and had no money.<sup>30</sup> Siqueiros suggested that Margáin allow artists to pay their taxes with artwork since that was “the only thing” they had.<sup>31</sup> Moreover, since their artwork was valuable, Siqueiros contended that the works would establish a significant collection for the nation.<sup>32</sup> Intrigued and “sensitive to the situation of artists,”<sup>33</sup> Margáin eventually presented the proposal to Antonio Carrillo Flores, the Secretary of the SHCP, who approved of the unusual scheme.<sup>34</sup> In November 1957, Margáin implemented the *Pago en Especie* program and collected the SHCP’s first payment of income taxes in art.<sup>35</sup>

In general, the Mexican art community received the establishment of *Pago en Especie* positively. In one of the first articles to announce the program, J. J. Crespo de la Serna heralded *Pago en Especie* as an “extraordinarily ingenious” initiative that had “characteristics of a real discovery.”<sup>36</sup> Almost in anticipation of potential skeptics, Crespo de la Serna carefully explained that *Pago en Especie* would both satisfy the tax obligations of artists as well as enrich the holdings of Mexico’s national heritage.<sup>37</sup> In his view, artists were not escaping a duty to the nation, but instead were contributing in a manner distinct from other professions:

[P]ainters, engravers, [and] sculptors are not what is known commonly as “practical people,” . . . who have their feet on the ground and know how to function . . . like everyone else. Some are bohemian, others forgetful, [and] the rest indifferent. All, more or less, walk amongst the clouds, where perhaps they draw their best inspiration. How can you require that they give an account of what they earn with their artistic products? . . . There are gaps in their calculations, disorder, and so on . . . As such[,] . . . the present [D]irector of Income Tax, . . . Hugo Margáin[, has decided] . . . to remedy that irregular situation by proposing that, according to unbiased estimates of the profits of each artist, an artist will not have to worry about archiving duplicated documents, nor carrying logbooks[;] rather, he must submit in kind, that is to say in his own artwork[,] the equivalent of his taxes.<sup>38</sup>

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<sup>30</sup> See Ganado Kim, *supra* note 2, at i (describing Siqueiros’s vigorous defense of artists); Garduño, *supra* note 2, at 232 (recounting the colorful encounter).

<sup>31</sup> Garduño, *supra* note 2, at 232.

<sup>32</sup> Ganado Kim, *supra* note 2, at i.

<sup>33</sup> See Sobrino Figueroa, *supra* note 8, at 31 (relating how Margáin was receptive to the proposal and continued discussions with Murillo and Siqueiros).

<sup>34</sup> Ganado Kim, *supra* note 2, at i.

<sup>35</sup> Sobrino Figueroa, *supra* note 8, at 31; see also San Cristóbal Larrea, *supra* note 10, at 38 (explaining that Margáin oversaw the first collection of art from 1957 to 1958).

<sup>36</sup> J. J. Crespo de la Serna, *Novedad: Los Pintores Pagan con Cuadros Sus Impuestos. Resultado: Afluyen las Obras para Fundar un Museo de Arte Moderno Mexicano*, MÉXICO EN LA CULTURA: SUPLEMENTO DE NOVEDADES, Nov. 10, 1957, at 6.

<sup>37</sup> *Id.*

<sup>38</sup> *Id.*

Beneath the extraordinary generalizations and condescending stereotypes, Crespo de la Serna essentially argued that, because the artistic profession was unique, it did not make sense to include artists in a traditional income tax system; instead, a special tax program was necessary.<sup>39</sup> He therefore praised the “realistic and advanced spirit” in which the SHCP had conceived of *Pago en Especie* to accommodate artists and exempt them from regular tax burdens.<sup>40</sup>

In addition to Siqueiros and Murillo, other important artists of the day rallied around *Pago en Especie*.<sup>41</sup> One of the program’s earliest and most illustrious advocates was Diego Rivera.<sup>42</sup> As a generous supporter of Mexican art and cultural heritage, Rivera had previously given the nation an entire collection of pre-Hispanic art.<sup>43</sup> Although he died the same year that Margáin implemented *Pago en Especie*, he fully embraced the tax scheme as a means to spur the growth of contemporary art in Mexico.<sup>44</sup> Before he passed away, Rivera even presented Margáin with three important paintings to add to the first collection of art in 1957.<sup>45</sup> In light of his past generosity to Mexico, this offer was an extraordinary demonstration of Rivera’s support for *Pago en Especie*. He was simply determined to be a part of the program—in spite of the fact that he did not owe any taxes.<sup>46</sup> In fact, when Margáin told him this, Rivera responded resolutely, “If I do not owe taxes, take the paintings as a donation.”<sup>47</sup>

Rivera’s enthusiasm for the program inspired other renowned artists to demonstrate their support of *Pago en Especie*.<sup>48</sup> By the time Crespo de la Serna announced the program in *Novedades* on November 10, 1957, Rufino Tamayo had already contributed *Venus Fotogénica* and Adolfo Best Maugard had given *The Head of Zapata*.<sup>49</sup> Moreover, Siqueiros, Murillo, and Juan Olgüíbel had also indicated that they were in the process of creating works for the program.<sup>50</sup> Thus, artists supported *Pago en Especie* from the beginning; even Rivera, Tamayo, Siqueiros, and Murillo—who may have been able to pay their income taxes in

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<sup>39</sup> *Id.*

<sup>40</sup> *Id.*

<sup>41</sup> See San Cristóbal Larrea, *supra* note 10, at 37 (listing many of the Mexican artists who embraced the program).

<sup>42</sup> See Sobrino Figueroa, *supra* note 8, at 31 (explaining that, despite his deteriorating health, Rivera “enthusiastically” endorsed the program).

<sup>43</sup> *Id.* at 32; Crespo de la Serna, *supra* note 36.

<sup>44</sup> See Sobrino Figueroa, *supra* note 8, at 31 (describing how Rivera wanted to participate in this “fiscal and cultural initiative,” which would assemble an “important collection of contemporary art”).

<sup>45</sup> *Id.* at 32; see also Ganado Kim, *supra* note 2, at ii (noting that these included *Estudio del Artista*, *Paisaje Urbano* and *Conteniendo el Hielo del Danubio en Bratislava*).

<sup>46</sup> Sobrino Figueroa, *supra* note 8, at 32.

<sup>47</sup> *Id.*

<sup>48</sup> *Id.*

<sup>49</sup> Crespo de la Serna, *supra* note 36.

<sup>50</sup> *Id.*



cash—wanted to participate to ensure the success of a payment-in-kind tax scheme for artists.

Many hoped that the *Pago en Especie* collection would form the foundation for an art museum supported, in part, by the SHCP.<sup>51</sup> Such an aspiration may have also contributed to the program's popularity among artists and encouraged submissions of superior quality. The early submissions reflected the artistic landscape of twentieth-century Mexico, and included works ranging from “figurative realism” to “more subjective and abstract” forms of expression.<sup>52</sup> By 1958, the government organized a public exhibition of the *Pago en Especie* collection at the SHCP, showcasing Rivera's three paintings as well as the other collected artwork.<sup>53</sup> Thus, after only one year, the plans for establishing a national collection from the nascent program seemed very promising.

### B. *The Legal Foundation and Early Operation of Pago en Especie*

Despite the fact that the SHCP had publicly implemented *Pago en Especie* under Margáin in 1957, formal legislation was not enacted for another eighteen years.<sup>54</sup> During that period, the program appears to have languished somewhat.<sup>55</sup> However, on June 3, 1975, President Luis Echeverría Álvarez signed the *Decreto que Autoriza el Pago en Especie del Impuesto al Ingreso de las Personas Físicas que Causen Quienes Produzcan Obras de Artes Plásticas* (Decree of 1975), which authorized creators of visual artwork to fulfill their income tax obligations by making payments in the form of their artwork.<sup>56</sup> Margáin has been credited with urging the government to finally legalize and revive the program after he became Secretary of the SHCP in 1970; however, due to an alleged disagreement with the President, the law authorizing *Pago en Especie* was not passed until after Margáin's departure from the SHCP in 1973.<sup>57</sup>

The Decree of 1975 formalized how *Pago en Especie* would function. First, it authorized the SHCP to receive all of the artwork collected annually.<sup>58</sup>

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<sup>51</sup> See *id.* (detailing how the art collected under *Pago en Especie* would help form an art museum); Garduño, *supra* note 2, at 235-36 (explaining that *Pago en Especie* was designed with a future museum of modern art in mind).

<sup>52</sup> San Cristóbal Larrea, *supra* note 10, at 38.

<sup>53</sup> Sobrino Figueroa, *supra* note 8, at 33.

<sup>54</sup> Ganado Kim, *supra* note 2, at ii.

<sup>55</sup> See *id.* (“During this lapse there is no record of more contributions of payment in kind.”); Garduño, *supra* note 2, at 237 (observing that, in spite of the initial media attention in 1957, the program was not formally legalized until the 1970s).

<sup>56</sup> Decreto que Autoriza el Pago en Especie del Impuesto al Ingreso de las Personas Físicas que Causen Quienes Produzcan Obras de Artes Plásticas, Diario Oficial de la Federación [DOF], 03-06-1975 (Mex.) [hereinafter Decree of 1975], [http://dof.gob.mx/nota\\_detalle.php?codigo=4758821&fecha=06/03/1975](http://dof.gob.mx/nota_detalle.php?codigo=4758821&fecha=06/03/1975) [https://perma.cc/66CE-T9]2].

<sup>57</sup> Garduño, *supra* note 2, at 237.

<sup>58</sup> Decree of 1975, *supra* note 56, art. 1.

Second, it restricted those who could participate in the program: only “artists who produce[d] works of visual art in an independent manner” qualified.<sup>59</sup> Although this excluded artists who produced commercial goods, the definition was still very broad. Any visual artist—regardless of his or her prestige in the art world or the quality of his or her work—could opt to pay in kind.<sup>60</sup> Third, the Decree of 1975 stipulated that a committee of representatives from the SHCP, the Secretary of Public Education, and the Secretary of National Patrimony (the committee) would oversee the submission of the artwork.<sup>61</sup> The committee was required to designate specialists to help it select and value the works of participating artists.<sup>62</sup>

Within this framework, an artist choosing to participate in *Pago en Especie* first had to submit an application to the SHCP.<sup>63</sup> If the SHCP determined that the applicant was an artist and complied with all of the requirements, he could offer his artwork to the committee.<sup>64</sup> With the help of specialists, the committee would review the artist’s proffered works.<sup>65</sup> If the artist was dissatisfied with either the committee’s “selection or valuation” of his works, he could withdraw his application and pay his income taxes with cash instead.<sup>66</sup>

After the Decree of 1975, many artists sought to pay their taxes through *Pago en Especie*,<sup>67</sup> including many who “already enjoyed high demand and visibility in the art world.”<sup>68</sup> In light of this revival, the ever growing collection eventually needed a designated place to store and exhibit the artwork. In 1994, the SHCP, which administered the holdings of *Pago en Especie*, created the Museo de Arte de la SHCP at the Antiguo Palacio del Arzobispado in Mexico City to house the permanent collection.<sup>69</sup>

### C. *The Contemporary Operation of Pago en Especie*

#### 1. The Application Process

Since 1975, subsequent decrees have altered the manner in which *Pago en Especie* functions, but giving artists a payment-in-kind option remains the

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<sup>59</sup> *Id.*

<sup>60</sup> The Decree of 1975 made no mention of whether part-time artists qualified. Presumably, part-time artists would have had to pay taxes on income earned from other jobs, but could have satisfied the taxes owed on the sale of artwork in this same manner.

<sup>61</sup> Decree of 1975, *supra* note 56, art. 3.

<sup>62</sup> *Id.*

<sup>63</sup> *Id.* art. 4.

<sup>64</sup> *Id.*

<sup>65</sup> *Id.* arts. 2-3.

<sup>66</sup> *Id.* art. 5.

<sup>67</sup> Ganado Kim, *supra* note 2, at iv.

<sup>68</sup> Garduño, *supra* note 2, at 237.

<sup>69</sup> Ganado Kim, *supra* note 2, at xi; Sobrino Figueroa, *supra* note 8, at 34.

primary objective. The most notable change in the process has been the adoption of a “sliding scale” payment formula, which allows artists to easily calculate how many pieces of art they owe each year.<sup>70</sup> Instead of depending on the committee to estimate an artist’s income and value his proffered works, now the number of works an artist sells in a given tax year pre-determines the number of works owed to the SHCP.<sup>71</sup> The Decree of 1994 fixed the proportion as follows:

Table 1: Number of Works an Artist Owes the SHCP in a Given Year<sup>72</sup>

Number of Works the Artist Sold	Numbers of Works the Artist Must Render to the SHCP
1 to 5 works	1 work
6 to 8 works	2 works
9 to 11 works	3 works
12 to 15 works	4 works
16 to 20 works	5 works
21+ works	6 works

Still in effect today, this sliding scale simplified the onerous and subjective process of valuing an artist’s works and thus altered the role of the committee, as discussed further below.

In addition to clarifying how many pieces of artwork an artist will owe annually, the Decree of 1994 further explained the SHCP’s application and selection process. First, an artist must notify the SHCP in writing of his desire to opt into *Pago en Especie* between January and April of a given year.<sup>73</sup> Although this registration does not bind an artist to the program if he decides to pay in cash in a subsequent tax year, it is necessary to participate in *Pago en Especie*.<sup>74</sup> After registering, an artist must declare how many of his works were sold the previous year and submit the works that he proposes to render to the collection.<sup>75</sup> All paintings and graphics must be signed, dated, and framed, with all necessary wires and screws; graphics must additionally carry

<sup>70</sup> Chris Hawley, *In Mexico, Artists Can Pay Their Taxes with Artwork*, USA TODAY (Apr. 16, 2010, 4:49 AM), [http://usatoday30.usatoday.com/news/world/2010-04-15-paying-taxes-with-artwork\\_N.htm](http://usatoday30.usatoday.com/news/world/2010-04-15-paying-taxes-with-artwork_N.htm) [<https://perma.cc/5LST-7N6F>]; see also Johnson, *supra* note 14 (explaining the logistics of the sliding scale).

<sup>71</sup> See Decree of 1994, *supra* note 12, art. 2 (providing the number of paintings an artist must submit).

<sup>72</sup> The numbers in this table have been reproduced from the Decree. *Id.*

<sup>73</sup> See *id.* art. 4 (indicating that this notice suffices until the artist submits a notice of withdrawal).

<sup>74</sup> *Id.*; see also Hawley, *supra* note 70 (noting that as of 2010, about 700 artists had registered and submitted examples of their work to the committee, though they do not all pay their taxes in kind every year).

<sup>75</sup> Decree of 1994, *supra* note 12, art. 4.

a unique identification number.<sup>76</sup> Likewise, sculptures must be signed, dated, and have a unique identification number.<sup>77</sup>

After the committee receives an applicant's submitted works, it makes no attempt to calculate whether the art's value is equal to the income tax owed. Likewise, the committee casts no judgment on the quality of the art, reasoning that both artists "with prodigious talent" and "artists who sell their work at park fairs or in markets . . . have a right to take part in the program."<sup>78</sup> Finally, the committee makes no effort to censor the art, regardless of how graphic or provocative it is.<sup>79</sup> Rather, the committee—with the aid of specialists—carefully evaluates the submitted pieces to ensure that they are "representative" (in terms of size and technique) of the artist's body of work sold in the previous three years before accepting it as payment in kind.<sup>80</sup> If the committee does not find that the works are representative, or if it finds that the artist sold a greater number of works than he claimed in his application to the SHCP, the artist may be permitted to offer other works or may be required to pay his income taxes in cash.<sup>81</sup>

## 2. The Type of Art Accepted

The Decree of 1994 only issued instructions for the submission of paintings, graphics, and sculptures to the committee,<sup>82</sup> meaning that other forms of art did not qualify as payment in kind; nonetheless, subsequent changes have broadened the type of media accepted under *Pago en Especie*.<sup>83</sup> On November 28, 2006, for instance, a new decree allowed all visual artists to participate, as long as their work was not industrial, artisanal, utilitarian, cinematic, applied, or architectural in nature.<sup>84</sup> As a result, digital and virtual art forms were finally eligible, and photography was officially sanctioned.<sup>85</sup> As of 2007, *Pago en Especie* had even accepted around ten installation projects on the reasoning

<sup>76</sup> *Id.*

<sup>77</sup> *Id.*

<sup>78</sup> Johnson, *supra* note 14.

<sup>79</sup> See Hawley, *supra* note 70 (giving examples of some of the "edgier" pieces of accepted art).

<sup>80</sup> Decree of 1994, *supra* note 12, arts. 2, 5; see also Johnson, *supra* note 14 (quoting Cristina López Beltrán, one of the administrators of *Pago en Especie*, who explained the role of the committee: "More than evaluate the monetary value of a work, the experts decide if the work is representative of the artist's oeuvre").

<sup>81</sup> Decree of 1994, *supra* note 12, art. 6.

<sup>82</sup> *Id.* arts. 1, 4.

<sup>83</sup> See MacMasters, *supra* note 11 (discussing the evolution of media requirements over time).

<sup>84</sup> Decreto por el que Se Otorgan Diversos Beneficios Fiscales a los Contribuyentes que Se Indican y Se Modifican los Diversos Publicados el 5 de Marzo de 2003 y el 31 de Octubre de 1994, Diario Oficial de la Federación [DOF], 28-11-2006, (Mex.) [hereinafter Decree of 2006], [http://dof.gob.mx/nota\\_detalle.php?codigo=4938574&fecha=28/11/2006](http://dof.gob.mx/nota_detalle.php?codigo=4938574&fecha=28/11/2006) [<https://perma.cc/ZJ6X-V57D>].

<sup>85</sup> MacMasters, *supra* note 11; see also Johnson, *supra* note 14 ("In recent years photography has been included in the program.").

that, despite their inherently ephemeral nature, their physicality made them similar to sculptural forms.<sup>86</sup> In light of these changes, some predict that the program will eventually embrace alternative art, performance art, and videos.<sup>87</sup>

### 3. A Mandate to Share the Collection

Finally, the Decree of 1994 emphasized the importance of sharing the *Pago en Especie* collection throughout Mexico in a spirit of federalism.<sup>88</sup> To accomplish this, it gave one-third of the entire *Pago en Especie* collection to the federal states.<sup>89</sup> Although the permanent collection still remains in the Antiguo Palacio del Arzobispado in Mexico City,<sup>90</sup> the SHCP must work with the National System of Fiscal Coordination to distribute other works received under *Pago en Especie* throughout the country.<sup>91</sup> In this way, the Decree of 1994 broadened the reach of the program, endeavoring “to enrich [the] cultural heritage and promote artistic values in the national territory.”<sup>92</sup>

But who determines what artwork goes where? After reviewing all of the works submitted to *Pago en Especie* in a given year,<sup>93</sup> the committee selects those “of a particularly high caliber” to become part of Mexico’s national patrimony.<sup>94</sup> This distinction means that the artwork is among the most significant artistic expressions of the nation and, as such, will be featured in the permanent collection in Mexico City.<sup>95</sup> Works that are not selected as national patrimony are then “divided up and shipped across the country to fill public museums and administrative buildings.”<sup>96</sup> Additionally, *Pago en Especie* pieces are frequently shared with museums around the world: in 2013, *Pago en Especie* shipped artwork to “[thirteen] international galleries.”<sup>97</sup>

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<sup>86</sup> MacMasters, *supra* note 11 (interviewing the Deputy Director of the Control of the Collections regarding these acquisitions).

<sup>87</sup> *See id.* (describing a new “openness” towards such art forms, which were not traditionally accepted by *Pago en Especie*); *see also* Johnson, *supra* note 14 (“[T]he tax service [i]s studying whether other kinds of artistic expression might be included, perhaps theater or performance art, which would be recorded and shown time after time.”).

<sup>88</sup> *See* Ganado Kim, *supra* note 2, at ix (examining the purposes specified in the Decree’s preamble).

<sup>89</sup> Decree of 1994, *supra* note 12, art. 8.

<sup>90</sup> Ganado Kim, *supra* note 2, at xi; Hershaw, *supra* note 13.

<sup>91</sup> *See* Decree of 1994, *supra* note 12, art. 8 (explaining that these entities will hold a lottery to allocate the works to different federal entities).

<sup>92</sup> *Id.* p.mbl.; *see also* Ganado Kim, *supra* note 2, at ix (claiming that the Decree of 1994 created a “more equitable” division of the artwork).

<sup>93</sup> Decree of 1994, *supra* note 12, arts. 5, 11; Ganado Kim, *supra* note 2, at x.

<sup>94</sup> Hershaw, *supra* note 13.

<sup>95</sup> *See id.* (explaining that the highest quality art enters the “national-heritage collection” displayed at the SHCP’s museum).

<sup>96</sup> *Id.*

<sup>97</sup> *Id.*

The Decree of 1994 also gave the SHCP the authority to sell less culturally significant works through an auction and use the proceeds to conserve and exhibit the rest of the collection.<sup>98</sup> However, it does not appear that such an auction has ever occurred.<sup>99</sup> Perhaps this is because an auction could be perceived as a rejection of the collection's "less desirable" art and discourage artists from participating in the program. Regardless, now the SHCP recognizes that it cannot sell any works because they are all part of Mexico's cultural heritage and because "[i]f the government made a profit, it would have to give the artists a tax refund."<sup>100</sup> Despite these practical limits on alienation, by allowing the SHCP to give some of the artwork to the states, the Decree of 1994 significantly extended the reach of *Pago en Especie* and enabled both Mexican and international audiences to enjoy the work of contemporary Mexican artists.

#### D. *Justifications for Pago en Especie*

Today, *Pago en Especie* continues to enjoy the support of the Mexican art community and the tax-paying public at large. There are many reasons for this, including the ease of payment<sup>101</sup> and the collective pride in the ever-growing national collection.<sup>102</sup> However, *Pago en Especie*'s success among the "[h]undreds of artists" who participate in the program annually<sup>103</sup> may also stem from its recognition that artists often have distinctly "irregular cash flows," which could affect their ability to pay taxes in cash.<sup>104</sup> For example, a sculptor has to buy huge blocks of stone and carve for many months before he can accumulate enough pieces to put on a gallery show and sell them.<sup>105</sup> Likewise, a painter may exhibit at her gallery every two or three years, but it could take her two or three years to amass all of that work in the first place; she may then enjoy a period of sales, but ultimately she has to return—literally—to the drawing board.<sup>106</sup> Thus, submitting artwork instead of cash significantly ameliorates

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<sup>98</sup> Decree of 1994, *supra* note 12, art. 11.

<sup>99</sup> See Ganado Kim, *supra* note 2, at x.

<sup>100</sup> Hawley, *supra* note 70.

<sup>101</sup> See *supra* subsection I.C.1.

<sup>102</sup> See, e.g., Johnson, *supra* note 14 (recounting interviews with artists who praised the program); Marcela Ojeda, *El Programa 'Pago en Especie' para Artistas Plásticos Cumple 57 Años*, EDUCACIÓN CONTRACORRIENTE (Mar. 31, 2014), <http://www.educacioncontracorriente.org/secciones/economia/23390-el-programa-pago-en-especie-para-artistas-plasticos-cumple-57-anos> [<https://perma.cc/F4JC-CFME>] (quoting the program director, San Cristóbal Larrea, who believes *Pago en Especie* has created Mexico's premier contemporary art collection).

<sup>103</sup> Johnson, *supra* note 14.

<sup>104</sup> Telephone Interview with Carmen Melián, Principal of Melián Arts, Former Director and Senior Specialist of Latin American Art at Sotheby's (Dec. 2, 2014) (on file with author).

<sup>105</sup> *Id.*

<sup>106</sup> *Id.*

artists' cash flow irregularities and may explain *Pago en Especie*'s continued popularity among artists today.

In addition to accommodating artists' cash flow difficulties, the Mexican government has repeatedly justified *Pago en Especie* as a means of collecting cultural touchstones that reflect Mexico's national heritage.<sup>107</sup> For example, the Decree of 1975 declared that *Pago en Especie*'s main purpose was "to protect and enhance the property and values that constitute the cultural heritage of the Nation and to make them accessible to the community."<sup>108</sup> To accomplish that goal, the Mexican government authorized the SHCP to collect a "representative sample of the visual arts" and exhibit these works as an "example of the national artistic creation of our time."<sup>109</sup> In this way, the *Pago en Especie* collection is an ever-growing inheritance for Mexico's future generations.

Viewing *Pago en Especie* as a way to cultivate cultural consciousness has remained the dominant justification for the program in the SHCP. The SHCP's current General Director of Cultural Promotion, Public Works, and Patrimonial Cultural Property, José Ramón San Cristóbal Larrea, has explained, "The artistic patrimony of Mexico is a social construction that affirms our identity. The richness of its tangible and intangible expressions has created countless symbols that reinforce our cultural ties . . . [and] national essence."<sup>110</sup> Other SHCP publications have described *Pago en Especie* as a means of harnessing the contemporary expression of Mexico's "ancestral roots."<sup>111</sup> However, the SHCP recognizes that the collection cannot reinforce cultural identity unless it is shared; as such, "[t]he purpose of the collection is not to hoard it, but rather to disseminate it nationally and internationally."<sup>112</sup> Hence, the SHCP frequently exhibits *Pago en Especie* works throughout Mexico and loans others to institutions around the world.<sup>113</sup>

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<sup>107</sup> For more information about how different countries conceive of cultural property and art, see John Henry Merryman, *Two Ways of Thinking About Cultural Property*, 80 AM. J. INT'L L. 831, 831-32 (1986). Merryman famously argued that two perspectives of cultural property divide the art world: a cosmopolitan view and a nationalist view. *Id.* Whereas a cosmopolitan view regards cultural property as part of humanity's "common" culture (irrespective of its original or current ownership), a nationalist view "implies the attribution of national character to objects," making them part of a "national cultural heritage." *Id.* In Mexico, a nationalist view appears to prevail.

<sup>108</sup> Decree of 1975, *supra* note 56, pmb.

<sup>109</sup> *Id.*

<sup>110</sup> San Cristóbal Larrea, *supra* note 10, at 34.

<sup>111</sup> See GANAMOS TODOS: SECRETARÍA DE HACIENDA Y CRÉDITO PÚBLICO, COLECCIÓN PROGRAMA PAGO EN ESPECIE 8 (2006) [hereinafter GANAMOS TODOS] ("The experimentation of a shared past, as well as the exploration of present development are two reasons for our pride in the ancestral roots of our culture. Contemporary art emerges from the trust in its traditions, in a synthesis that has been achieved through modernity.")

<sup>112</sup> MacMasters, *supra* note 11.

<sup>113</sup> See, e.g., GANAMOS TODOS, *supra* note 111, at 8 (explaining how *Pago en Especie* has exhibited works domestically and abroad); Johnson, *supra* note 14 (noting exhibitions in Turkey, Israel, India, Georgia, Venezuela, Thailand, Bolivia, and Saudi Arabia).

Overall, *Pago en Especie* remains a popular fixture in Mexico's tax system. It not only resolves artists' unpredictable cash flows in an innovative and straightforward manner, but also provides a domestic and international platform for celebrating the uniqueness of Mexican art and culture. In this way, *Pago en Especie* highlights Mexico's contemporary artwork as touchstones that link the past, present, and future of the country.

## II. THE UNITED KINGDOM'S CULTURAL GIFTS SCHEME

### A. *The Origins of the Cultural Gifts Scheme*

The United Kingdom has a long tradition of allowing taxpayers to decrease their inheritance taxes by bequeathing cultural property to the state through a program called Acceptance in Lieu (AIL).<sup>114</sup> David Lloyd George, then the Chancellor of the Exchequer, first laid the groundwork for the program in the Finance Act of 1910, which enabled estates to settle their inheritance taxes in part or in whole by offering land to the nation.<sup>115</sup> The tax commissioners were permitted to "hold any property . . . [and] deal with it in such manner as Parliament may hereafter determine."<sup>116</sup> Over the next century, Parliament expanded this practice to allow estates to satisfy their enormous inheritance taxes with valuable cultural property or artwork.<sup>117</sup> These works were then placed in museums, archives, and libraries for public viewing.<sup>118</sup>

AIL is still in effect today. Once an estate transfers ownership of artwork to the public, it is able to reduce its inheritance taxes.<sup>119</sup> It appears to function like a tax credit: "The amount of tax satisfied is the open market value of the item less the Inheritance Tax that would have been payable (the current rate of tax is 40%) plus 25% of the notional tax, known as the *douceur*."<sup>120</sup> To illustrate how advantageous this is, the Department for Culture, Media and Sport has estimated that generally, an object is worth "17% more if offered in

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114 MUSEUMS, LIBRARIES & ARCHIVES COUNCIL, ACCEPTANCE IN LIEU: REPORT 2009/2010, at 2, 5 (2010) [hereinafter AIL: REPORT 2009/2010], [http://www.artscouncil.org.uk/media/uploads/pdf/mla\\_cultural\\_property/AIL\\_report\\_2010.pdf](http://www.artscouncil.org.uk/media/uploads/pdf/mla_cultural_property/AIL_report_2010.pdf) [https://perma.cc/6NEB-Y28P].

115 *Id.*; Finance Act 1910, 10 Edw. 7 c. 8, § 56(1) (Eng.), [http://www.legislation.gov.uk/ukpga/1910/8/pdfs/ukpga\\_19100008\\_en.pdf](http://www.legislation.gov.uk/ukpga/1910/8/pdfs/ukpga_19100008_en.pdf) [https://perma.cc/4N8Z-8S2Y].

116 Finance Act 1910, 10 Edw. 7 c. 8, § 56(3) (Eng.).

117 AIL: REPORT 2009/2010, *supra* note 114, at 2, 5.

118 *Government Accepts Works of Art in Lieu of £125 Million in Tax Payments*, TELEGRAPH (Sept. 10, 2014), <http://www.telegraph.co.uk/finance/personalfinance/tax/11088299/Government-accepts-works-of-art-in-lieu-of-125-million-in-tax-payments.html> [https://perma.cc/WSY9-49A3].

119 See Paul Huggins, *How Art Can Help You Keep the Cuts at Bay: While Western Governments Wrestle with Austerity Economics, Tax Concessions on Art Remain Generous*, 24 ART NEWSPAPER, no. 261, Oct. 2014, at 1, 19.

120 *Id.*



lieu of tax than if sold on the open market at the same price . . . because tax must be paid on the selling price.”<sup>121</sup>

Not all objects, however, qualify for AIL. The Acceptance in Lieu Panel (AIL Panel), which consists of independent experts,<sup>122</sup> evaluates every object offered in place of inheritance tax.<sup>123</sup> To qualify, the object must be preeminent, meaning that it must be “of particular significance either individually or collectively when displayed in a public collection or important historic building.”<sup>124</sup>

The longevity and success of AIL suggest that the United Kingdom has come to view taxation as a means of augmenting not only the Treasury, but also the nation’s cultural landscape. In fact, Sir Peter Bazalgette (the Chair of Arts Council England) recently acknowledged that AIL reflects both of these policy objectives: in 2013, he championed the program for “enabl[ing] those paying inheritance tax both to meet their obligations and to enrich the national culture by transferring works of art and valuable objects to our museums and libraries.”<sup>125</sup> In light of AIL’s strong record, it is not surprising that the United Kingdom recently created another tax program to ensure that the arts will continue to “resonate and inspire down the centuries.”<sup>126</sup>

#### B. *The Formation and Contemporary Operation of the Cultural Gifts Scheme*

After considerable lobbying from the art community,<sup>127</sup> the Finance Act of 2012 authorized an addition to the AIL program,<sup>128</sup> and in March 2013 the United Kingdom implemented CGS.<sup>129</sup> CGS is novel because it permits taxpayers to reduce their income tax, capital gains tax, or corporation tax by

<sup>121</sup> DEP’T FOR CULTURE, MEDIA & SPORT, 2010 TO 2015 GOVERNMENT POLICY: MUSEUMS AND GALLERIES app. 1 (2015), <https://www.gov.uk/government/policies/maintaining-world-leading-national-museums-and-galleries-and-supporting-the-museum-sector/supporting-pages/letting-people-donate-items-of-cultural-and-historical-importance-to-the-state-in-return-for-tax-reductions-acceptance-in-lieu-scheme> [<https://perma.cc/8E3L-FUSX>].

<sup>122</sup> See ARTS COUNCIL ENG., CULTURAL GIFTS SCHEME 3, <http://www.artscouncil.org.uk/media/uploads/pdf/FinalCGSLeaflet.pdf> [<https://perma.cc/3MG2-X4ZB>] (“The [AIL] Panel consists of independent experts, who seek specialist advice—generally from museum curators, scholars and members of the art trade—on the object offered.”); see also ARTS COUNCIL ENG., AIL PANEL MEMBERS, [http://www.artscouncil.org.uk/media/uploads/AIL\\_PANEL\\_MEMBERS\\_2015\\_09.docx](http://www.artscouncil.org.uk/media/uploads/AIL_PANEL_MEMBERS_2015_09.docx) [<https://perma.cc/36KG-Q8SB>] (providing information about the experts who currently sit on the AIL Panel, which is chaired by Edward Harley).

<sup>123</sup> CULTURE, MEDIA & SPORT COMM., PROTECTING AND PRESERVING OUR HERITAGE (VOLUME II: WRITTEN EVIDENCE), 2006, HC 912-II, at Ev. 2 (UK), <http://www.publications.parliament.uk/pa/cm200506/cmselect/cmcomeds/912/912ii.pdf> [<https://perma.cc/BA6S-CW6E>].

<sup>124</sup> Huggins, *supra* note 119, at 19.

<sup>125</sup> AIL: REPORT 2013, *supra* note 17, at 4.

<sup>126</sup> *Id.*

<sup>127</sup> See Huggins, *supra* note 119, at 19 (noting that museums and galleries called for the government to provide income tax relief in exchange for art).

<sup>128</sup> Finance Act 2012, c. 14, sch. 14 (Eng.).

<sup>129</sup> AIL: REPORT 2013, *supra* note 17, at 4.

“gifting” cultural property and art to the United Kingdom *during their lifetime*, not just upon their death (as in AIL).<sup>130</sup> As Sir Bazalgette explained when CGS accepted its first object in 2013, “[CGS] is an important element in the Government’s range of tax incentives to encourage philanthropy, [because it] allows individuals and companies to reduce substantially their income or corporation tax liabilities, according to the value of the gift.”<sup>131</sup> Thus, by expanding the array of tax concessions to include income tax relief under CGS, the United Kingdom remains committed to using taxation as a means of enhancing its cultural landscape.

Significantly, both CGS and AIL operate within a budget that limits the amount of tax that can be written off in a given year. In 2013, both schemes had a combined £30 million limit, meaning that “[t]he total value of tax reductions available under the CGS and taxes offset under the AIL Scheme [could] not, together, exceed £30 million.”<sup>132</sup> Thus, the AIL Panel—which also oversees CGS applications—must be vigilant in calculating the value of the tax reductions to ensure that it does not exceed the budget.<sup>133</sup> Although the combined budget may initially appear restrictive, the Chairman of the AIL Panel has explained that “[h]aving a single budget . . . allows a flexibility which acknowledges that it will take some time to establish cultural gifts as part of the philanthropic planning arrangements of private donors.”<sup>134</sup> Perhaps to encourage taxpayers to use CGS in their tax plans, the government announced in March 2014 that it would increase the combined annual budget for AIL and CGS from £30 million to £40 million.<sup>135</sup>

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<sup>130</sup> Finance Act 2012, c. 14, sch. 14 (Eng.); AIL: REPORT 2013, *supra* note 17, at 4.

<sup>131</sup> AIL: REPORT 2013, *supra* note 17, at 4.

<sup>132</sup> DEP’T FOR CULTURE, MEDIA & SPORT, GUIDANCE NOTES ON THE CULTURAL GIFTS SCHEME para. 9 (2011) [hereinafter DCMS: GUIDANCE NOTES 2011], [https://www.gov.uk/government/uploads/system/uploads/attachment\\_data/file/77838/Cultural\\_Gift\\_Scheme\\_Guidance1.pdf](https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/77838/Cultural_Gift_Scheme_Guidance1.pdf) [<https://perma.cc/77U6-KEH7>].

<sup>133</sup> See AIL: REPORT 2013, *supra* note 17, at 5 (recording the value of the objects accepted and the amount of tax settled annually from 2004 to 2013 in a table).

<sup>134</sup> *Id.* at 5-6.

<sup>135</sup> See CGS & AIL: REPORT 2014, *supra* note 18, at 5 (describing the budget increase as a “hugely encouraging development” after “another productive and rewarding year” for AIL and CGS); see also Elizabeth, *Good News for National Heritage Property in Today’s Budget Announcement*, ART & ARTIFICE (Mar. 19, 2014, 2:56 PM) [hereinafter *Good News*], <http://andalawblog.blogspot.com/2014/03/good-news-for-national-heritage.html> [<https://perma.cc/NL4P-TJ8S>] (discussing AIL and the addition of CGS, praising the budget increase, and exploring its implications).

### 1. The Application Process

The Department for Culture, Media and Sport has issued thorough instructions for the operation of CGS.<sup>136</sup> Arts Council England<sup>137</sup> oversees CGS with the assistance of the AIL Panel, which evaluates the items offered by taxpayers “on a first come, first served basis.”<sup>138</sup> To apply, a taxpayer must provide details about the object and its creator, a valuation, a record of any previous sales, proof of good legal title, a comprehensive provenance report (including information about the object from 1933 to 1945), three color photographs, an account of the present condition of the object, a declaration about why the object is preeminent, the owner’s proposed tax reduction schedule, and the name of the institution favored to receive the object.<sup>139</sup> Provided that all requisite information is included, each application will be registered within thirty days of submission.<sup>140</sup> The registration date is significant; even if the AIL Panel deliberates about an item’s value for a long period of time, the item is assessed at its fair market value as of the registration date.<sup>141</sup>

Once an application has been registered, the AIL Panel must determine whether the offered object is preeminent.<sup>142</sup> The Finance Act of 2012 clarified that a preeminent item includes

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<sup>136</sup> See, e.g., DEP’T FOR CULTURE, MEDIA & SPORT, CULTURAL GIFTS SCHEME: SCHEME AND GUIDANCE (2015) [hereinafter CGS: SCHEME AND GUIDANCE 2015], <http://www.artscouncil.org.uk/media/uploads/doc/CGSguidance27january2015.docx> [<https://perma.cc/WV82-TRJG>]; DEP’T FOR CULTURE, MEDIA & SPORT, CULTURAL GIFTS SCHEME: SCHEME AND GUIDANCE (2013) [hereinafter CGS: SCHEME AND GUIDANCE 2013], [http://www.artscouncil.org.uk/media/uploads/pdf/DCMS\\_Guidance\\_15\\_March.pdf](http://www.artscouncil.org.uk/media/uploads/pdf/DCMS_Guidance_15_March.pdf) [<https://perma.cc/TM69-LCUJ>].

<sup>137</sup> Arts Council England is an entity that supports “non-national” museums and galleries across England. DEP’T FOR CULTURE, MEDIA & SPORT, 2010 TO 2015 GOVERNMENT POLICY: MUSEUMS AND GALLERIES app. 4 (2015), <https://www.gov.uk/government/publications/2010-to-2015-government-policy-museums-and-galleries/2010-to-2015-government-policy-museums-and-galleries#appendix-4-funding-the-arts-council-to-provide-support-to-non-national-museums> [<https://perma.cc/7CLT-5LG7>]. As stated in its Royal Charter, one of Arts Council England’s main objectives is to “advance the education of the public and to further any other charitable purpose which relates to the establishment, maintenance and operation of museums and libraries (which are either public or from which the public may benefit) and to the protection of cultural property.” ARTS COUNCIL ENG., CONSOLIDATED ROYAL CHARTER para. 4(3) (1994), [http://www.artscouncil.org.uk/media/uploads/2013\\_Royal\\_Charter\\_2002.pdf](http://www.artscouncil.org.uk/media/uploads/2013_Royal_Charter_2002.pdf) [<https://perma.cc/MA2T-F82P>].

<sup>138</sup> CGS: SCHEME AND GUIDANCE 2015, *supra* note 136, para. 11(b).

<sup>139</sup> *Id.* para. 19.

<sup>140</sup> *Id.* para. 16.

<sup>141</sup> *Id.* paras. 16-17. Fair market value is defined as “the price at which the object could reasonably be expected to change hands in an open and unrestricted market, where buyer and seller are both knowledgeable, informed and prudent, with neither being under any compulsion to buy and sell and where the value is unaffected by any consideration relating to past or future transactions between the parties.” *Id.* para. 20.

<sup>142</sup> *Id.* paras. 7, 11.

(a) any picture, print, book, manuscript, work of art, scientific object or other thing that the relevant Minister is satisfied is pre-eminent for its national, scientific, historic or artistic interest,

(b) any collection or group of pictures, prints, books, manuscripts, works of art, scientific objects or other things if the relevant Minister is satisfied that the collection or group, taken as a whole, is pre-eminent for its national, scientific, historic or artistic interest, or

(c) any object that is or has been kept in a significant building if it appears to the relevant Minister desirable for the object to remain associated with the building.<sup>143</sup>

Significantly, preeminent objects may include works by living artists,<sup>144</sup> allowing for the submission of contemporary art.

In its final assessment of an application, the AIL Panel considers the object's preeminence, its fair market value, and the eligibility of the applicant's favored institution.<sup>145</sup> In addition, the AIL Panel must ensure that it does not exceed the limited annual budget for CGS and AIL.<sup>146</sup> The AIL Panel only recommends accepting an object if it meets all of the above conditions.<sup>147</sup>

## 2. Transferring Title in Return for a Tax Reduction

Once an object is accepted under CGS, the taxpayer must transfer title to the relevant Minister.<sup>148</sup> However, until the AIL Panel identifies an eligible institution willing to assume ownership, a third party institution may be entrusted with its temporary care and possession.<sup>149</sup> An eligible institution willing to receive a CGS object can be

(a) any museum, art gallery, library, archive or other similar institution having as its purpose or one of its purposes the preservation for the public benefit of a collection of historic, artistic or scientific interest; or

(b) any body having as its purpose or one of its purposes the provision, improvement or preservation of amenities enjoyed or to be enjoyed by the public.<sup>150</sup>

Because eligible institutions are required to provide public access to CGS objects,<sup>151</sup> CGS "provide[s] a route for works by important artists and creators to come into public ownership."<sup>152</sup>

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<sup>143</sup> Finance Act 2012, c. 14, sch. 14, pt. 4, para. 22 (Eng.).

<sup>144</sup> CGS: SCHEME AND GUIDANCE 2015, *supra* note 136, para. 13.

<sup>145</sup> *Id.* para. 26.

<sup>146</sup> *Id.*

<sup>147</sup> *Id.* para. 38.

<sup>148</sup> *Id.* para. 40.

<sup>149</sup> *Id.* para. 41.

<sup>150</sup> *Id.* para. 33.

<sup>151</sup> *Id.* paras. 35(c), 42(b).

<sup>152</sup> CGS & AIL: REPORT 2014, *supra* note 18, at 4.

If a taxpayer requests that the object go to a specific institution, the AIL Panel will attempt to fulfill that request.<sup>153</sup> If no request is made, Arts Council England will advertise the CGS object on its website and invite eligible institutions to apply for the object's permanent allocation, as it has done in the past with AIL.<sup>154</sup> If an institution accepts title to an object, it assumes the financial obligations of maintaining, conserving, and exhibiting the object and cannot sell or transfer it without the consent of the overseeing Minister.<sup>155</sup>

In exchange for transferring title to an object accepted under CGS, the government gives a reduction against income, capital gains, or corporation tax.<sup>156</sup> As with AIL, the benefits of a CGS tax reduction are significant. A taxpayer can reduce his income or capital gains taxes by up to thirty percent of the agreed fair market value of the accepted object.<sup>157</sup> A company can reduce its corporation tax liability by up to twenty percent of the object's agreed upon fair market value.<sup>158</sup> Once the reduction amount is determined, a taxpayer has limited discretion in employing the relief.<sup>159</sup> In some cases, he may entirely eliminate his income tax liability for that year;<sup>160</sup> alternatively,

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<sup>153</sup> See CGS: SCHEME AND GUIDANCE 2015, *supra* note 136, para. 35 (“The [AIL] Panel will consider any such preferred institution and take into account factors such as: (a) the institution's collections policy; (b) its existing holdings; (c) the level of public access that it will provide; (d) its ability to provide proper care and maintenance for the object; (e) its security and environmental controls; and (f) any connection it has to the owner, the object, or its creator.”).

<sup>154</sup> See *Items for Allocation: Items Accepted Under the Acceptance in Lieu Scheme and Available for Allocation*, ARTS COUNCIL ENG., <http://www.artscouncil.org.uk/what-we-do/supporting-museums/cultural-property/tax-incentives/items-allocation> [<https://perma.cc/UC2W-Y6C3>] (last visited Jan. 23, 2016) (listing any AIL and CGS items available for permanent allocation and providing application instructions). In 2014, the AIL Panel advertised several works by Frank Auerbach that had been accepted under AIL from the estate of Lucian Freud. See *Invitation for Permanent Allocation*, ARTS COUNCIL ENG., [http://www.artscouncil.org.uk/media/uploads/pdf/auerbach\\_groups\\_allocation\\_up\\_dated\\_171014.pdf](http://www.artscouncil.org.uk/media/uploads/pdf/auerbach_groups_allocation_up_dated_171014.pdf) [<https://perma.cc/4YEW-PEAD>] (last visited Jan. 23, 2016) (describing and providing pictures of the collected works). While no CGS gifts are currently listed for permanent allocation, the AIL Panel is presently soliciting applications for various items received under AIL in 2015. See *Items Available for Permanent Allocation*, ARTS COUNCIL ENG., <http://www.artscouncil.org.uk/media/uploads/pdf/2015AILReportAllocationsFinal.pdf> [<https://perma.cc/R6UV-QDJL>] (last visited Jan. 23, 2016) (identifying nine AIL items from the 2015 collection that await permanent placement, including artwork, a shoe collection, and an engine).

<sup>155</sup> CGS: SCHEME AND GUIDANCE 2015, *supra* note 136, para. 42.

<sup>156</sup> Finance Act 2012, c. 14, sch. 14, pt. 2, paras. 2, 12 (Eng.); CGS: SCHEME AND GUIDANCE 2015, *supra* note 136, paras. 40, 46.

<sup>157</sup> Finance Act 2012, c. 14, sch. 14, pt. 2, para. 4 (Eng.); CGS: SCHEME AND GUIDANCE 2015, *supra* note 136, paras. 11(h), 20-21.

<sup>158</sup> Finance Act 2012, c. 14, sch. 14, pt. 3, para. 14 (Eng.); CGS: SCHEME AND GUIDANCE 2015, *supra* note 136, paras. 11(h), 20-21.

<sup>159</sup> CGS: SCHEME AND GUIDANCE 2015, *supra* note 136, para. 11(h).

<sup>160</sup> See *id.* para. 51 (“For example, if an individual has a tax reduction available of £200,000 with an income tax liability of £100,000 and a capital gains tax liability of £300,000 the donor may specify the tax reduction to be set first against income tax and then against capital gains tax. In that case the whole of the income tax liability will be extinguished . . .”).

he may elect to “spread the tax reduction across up to five tax years,” provided that he and the AIL Panel agree upon a reduction schedule in advance.<sup>161</sup>

### 3. The First Gifts Accepted

In 2013, CGS accepted its first gift: a collection of John Lennon’s hand-written lyrics and letters.<sup>162</sup> As explained in Arts Council England’s 2013 Report, the AIL Panel determined that the lyrics and letters qualified as preeminent objects, were in satisfactory physical condition, and were valued in a fair manner.<sup>163</sup> With respect to their preeminence to the nation, the Arts Council said,

As one of the most commercially successful and critically acclaimed acts in the history of popular music, the Beatles’ cultural legacy is still very much apparent today . . . .

. . . These iconic papers provide a fascinating insight into Lennon’s personal life and the creative workings of his mind, not only as a songwriter but also as a writer and poet.<sup>164</sup>

The taxpayer who offered this collection, Hunter Davies, requested that it go to the British Library to be among treasures such as the Magna Carta, Shakespeare’s books, and Beethoven’s music.<sup>165</sup> Davies explained, “I want my Beatles collection to be kept together, in one place, and on public display . . . . I’m really pleased the Cultural Gifts Scheme has helped me make this a reality.”<sup>166</sup> Although Davies did not mention the favorable tax reduction that CGS offers, it was likely an important factor in his decision to apply to CGS.

Arts Council England accepted four more works under CGS in 2014.<sup>167</sup> One was a portrait by Vincent Van Gogh called *Tête de Paysanne* (*Head of a Peasant Woman*), which the donor wanted to give to the National Gallery since the museum did not have any of Van Gogh’s earlier portraits.<sup>168</sup> The three other gifts—*The Dinner Party* by Sam Walsh, *Portrait of Elizabeth Balguy* by Joseph

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<sup>161</sup> *Id.* para. 47; see also Finance Act 2012, c. 14, sch. 14, pt. 2, para. 3 (Eng.) (specifying that the five years must begin with “the tax year in which the offer registration date falls” and extend across only “the [four] tax years following that tax year”); Huggins, *supra* note 119, at 19 (noting that the reduction must be claimed “either in the year of the gift or in any of the next four tax years”).

<sup>162</sup> See AIL: REPORT 2013, *supra* note 17, at 64 (identifying the letters, postcards, and song lyrics included in the collection).

<sup>163</sup> *Id.*

<sup>164</sup> *Id.*

<sup>165</sup> *Id.*

<sup>166</sup> *Id.*

<sup>167</sup> CGS & AIL: REPORT 2014, *supra* note 18, at 4.

<sup>168</sup> *Id.* at 11; Elizabeth, *New Van Gogh Donated to the National Gallery Under the Cultural Gifts Scheme*, ART & ARTIFICE (Jan. 8, 2014, 9:00 AM), <http://andalawblog.blogspot.co.uk/2014/01/new-van-gogh-donated-to-national.html> [<https://perma.cc/X2C3-666U>].

Wright of Derby, and ninety-nine political posters from 1900 to 1924—were allocated to the Walker Art Gallery, the Holburne Museum, and the University of Bristol Library, respectively.<sup>169</sup> In an effort to highlight CGS’s “first full year of operation,”<sup>170</sup> Arts Council England’s 2014 Report identified the donors and documented how CGS allowed them to allocate their gift to a particular institution.<sup>171</sup> For instance, Jill Ford explained that it was meaningful to give her husband’s collection of political posters to the University of Bristol Library because she had attended school there and her husband had been the University Librarian.<sup>172</sup> By trying to honor taxpayers’ allocation requests, CGS allows taxpayers to leave a personal mark upon the cultural landscape of the nation and thus imbues tax reductions with greater meaning.

Although CGS is still in its infancy, the five gifts received from 2013 to 2014 are impressive. Rich in their historic and artistic significance, CGS celebrates how these diverse papers, paintings, and posters enhance the cultural holdings of the nation. As more taxpayers learn of this innovative way to reduce their income and capital gains taxes, CGS will likely receive more high-quality applications from taxpayers with preeminent objects in the coming years.

### *C. Justifications for the Cultural Gifts Scheme*

Proponents of CGS maintain that the program is important because it enhances the cultural landscape of the United Kingdom in a cost-efficient manner. Prior to CGS, taxpayers had no tax incentive to give charitable donations to museums.<sup>173</sup> Because of this, museums had to compete for valuable pieces in the marketplace.<sup>174</sup> Now, CGS provides a way for cultural institutions to secure such objects without raising the enormous funds necessary to purchase them; in fact, they will not have to pay at all. AIL has illustrated how advantageous this is for museums. From 2012 to 2013 AIL accepted objects with a fair market value of £50 million; as Sir Bazalgette thereafter noted, “If their sale had been on the open market, these works of art might have been lost to us forever: instead, . . . the[se] beautiful and fascinating objects . . . can

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<sup>169</sup> CGS & AIL: REPORT 2014, *supra* note 18, at 12-16.

<sup>170</sup> *Id.* at 4.

<sup>171</sup> *Id.* at 12-16.

<sup>172</sup> *Id.* at 16.

<sup>173</sup> See Salamander Davoudi & Vanessa Houlder, *Museums Cheer Art Donor Tax Break*, FIN. TIMES (Dec. 2, 2011, 10:14 PM), <http://www.ft.com/cms/s/0/d96a7abc-1ce9-11e1-a134-00144feabdc0.html#axzz3rJeSS7DI> [<https://perma.cc/X84D-GGHF>] (“Under the old scheme there was no incentive to give to a museum when you were alive. In order to help your tax bill you would sell on the open market.”).

<sup>174</sup> See *id.* (describing how art institutions have lobbied for “a cultural shift towards greater philanthropy” as an alternative means of acquiring important works).

now be enjoyed by the public.”<sup>175</sup> Like AIL, CGS gives cultural institutions access to an otherwise prohibitively expensive art market and helps ensure that the nation’s “museums and libraries [remain] vital places of enrichment.”<sup>176</sup> Because “the nation and its collections gain enormously—and in perpetuity—from such [tax] concessions,”<sup>177</sup> advocates champion CGS as a cultural coup.

A second justification for CGS is the prediction that the program will encourage tourism. In its 2014 Report, Arts Council England acknowledged that the objects accepted under CGS would “delight and inspire the many millions who visit [its] museums and collections.”<sup>178</sup> By permanently augmenting the United Kingdom’s cultural institutions with objects that resonate with people from all over the world,<sup>179</sup> CGS ensures that art lovers will have to come to the United Kingdom to see certain works.

Overall, although it is still a young program, CGS is quickly establishing itself as an indispensable scheme to both taxpayers and the government. Not only is it an “important element in the [United Kingdom’s] range of tax incentives to encourage philanthropy” among taxpayers, but it is also a cost-efficient way to cultivate the nation’s cultural landscape and secure a steady stream of tourists for generations to come.<sup>180</sup>

### III. TREATMENT OF ART AND ARTISTS UNDER THE UNITED STATES INCOME TAX SYSTEM

Before considering whether the United States should emulate *Pago en Especie* or CGS, it is imperative to survey how the federal income tax scheme currently treats art and artists.<sup>181</sup> In contrast to Mexico and the United Kingdom, artists and art owners cannot render paintings or sculptures to satisfy their

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<sup>175</sup> AIL: REPORT 2013, *supra* note 17, at 4.

<sup>176</sup> *Id.*

<sup>177</sup> *Id.*

<sup>178</sup> CGS & AIL: REPORT 2014, *supra* note 18, at 4.

<sup>179</sup> Unlike *Pago en Especie*, which only collects visual works made by “Mexican or foreign authors who obtain taxable income for their artistic activity in the country,” *see* Decree of 1975, *supra* note 56, pmb., CGS seeks to acquire *any* work considered preeminent for its “national, scientific, historic, or artistic” value, regardless of its creator’s nationality or its place of origin, *see* Finance Act 2012, c. 14, sch. 14, pt. 4, para. 22 (Eng.).

<sup>180</sup> AIL: REPORT 2013, *supra* note 17, at 4.

<sup>181</sup> This Comment does not address the role of art in estate taxes; however, that is another area where payment-in-kind programs should be evaluated. For example, New Mexico allowed the Georgia O’Keeffe estate to satisfy a portion of its state inheritance tax by giving artwork to state-run museums. *See* Email Interview with Elizabeth Glassman, President & CEO, Terra Foundation for American Art (Dec. 1, 2014) (on file with author). For a detailed analysis of payment-in-kind options for estates, *see* generally Anne-Marie Rhodes, *The Medium of Payment: An Option in Estate Tax Reform*, 57 NOTRE DAME L. REV. 285 (1981).



taxes. Instead, all federal income taxes have to be paid in money,<sup>182</sup> either “online, by phone, or by check or money order.”<sup>183</sup> Nonetheless, art can still secure significant tax privileges for a taxpayer, albeit in a less direct manner than in Mexico or the United Kingdom. Why is this? One possible explanation stems from the unique position that art occupies in the federal tax system: “Tax laws are designed to raise revenue and at the same time to serve a role of patronage. [As such, b]oth subtle and obvious inconsistencies have arisen in the federal tax laws as a result of the difficulties encountered in striking a balance between these two functions.”<sup>184</sup> Thus, while the United States collects revenue through money payments from all taxpayers, it simultaneously offers *indirect* tax benefits such as “deductions, credits, exclusions, exemptions, deferrals and preferential rates” to patronize the arts.<sup>185</sup>

The following discussion explores two ways in which the Internal Revenue Code (IRC) allows those who donate art and those who create art to claim certain deductions to reduce their taxable income. If an art collector donates artwork to a charitable organization, he may deduct either the artwork’s fair market value<sup>186</sup> or its basis<sup>187</sup> from his adjusted gross income (subject to

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182 The IRC requires the collection of taxes through “any commercially acceptable means . . . provided in regulations prescribed by the Secretary.” I.R.C. § 6311(a) (2012). The regulations currently indicate that checks, money orders, credit cards, and debit cards are permissible forms of payment. Treas. Reg. §§ 301.6311-1(a), -2(a) (as amended in 2001). Since art is not typically perceived as a “commercially acceptable means” of payment, it is very unlikely that the regulations could ever include art as a form of payment. This outcome is consistent with previous IRS interpretations:

There is no provision of Federal law under which taxes may be paid by a voluntary transfer of real or personal property to the Federal Government. Tangible property is not legal tender. . . . The clear intent of Federal law is that taxes are to be paid in money or its equivalent.

Rev. Rul. 76-350, 1976-2 C.B. 396, 1976 WL 36877, at \*1.

183 INTERNAL REVENUE SERV., 1040 INSTRUCTIONS: 2015, at 74 (2016), <http://www.irs.gov/pub/irs-pdf/i1040gi.pdf> [<https://perma.cc/LD6H-YMKP>].

184 Jeffrey C. McCarthy, *Federal Income Taxation of Fine Art*, 2 CARDOZO ARTS & ENT. L.J. 1, 2 (1983).

185 *Id.* at 2-3; see also ALAN L. FELD ET AL., PATRONS DESPITE THEMSELVES: TAXPAYERS AND ARTS POLICY 24 (1983) (“In the United States, local, state, and federal governments distribute indirect aid to the arts through tax expenditures—taxes that are ‘normally’ applicable but that governments do not collect because of deductions, credits, and exemptions.”).

186 The Treasury regulations define the fair market value of an object as “the price at which the property would change hands between a willing buyer and a willing seller, neither being under any compulsion to buy or sell and both having reasonable knowledge of relevant facts.” Treas. Reg. § 1.170A-1(c)(2) (2015). Significantly, the fair market valuation considers the specific market where the property is usually bought and sold. 2 LEONARD D. DUBOFF ET AL., THE DESKBOOK OF ART LAW, at N-35 (2d ed. 2006).

187 “The basis of property shall be the cost of such property.” I.R.C. § 1012(a); see also INTERNAL REVENUE SERV., PUB. NO. 551: BASIS OF ASSETS 2 (2014), <http://www.irs.gov/pub/irs-pdf/p551.pdf> [<https://perma.cc/MYS5-J4RA>] (“The basis of property you buy is usually its cost. The cost is the amount you pay in cash, debt obligations, other property, or services.”).

certain percentage restrictions).<sup>188</sup> For artists, the provisions are slightly less generous. If an artist donates her own artwork to a charity, she may only deduct the artwork's basis from her adjusted gross income; however, she may deduct any business expenses from her gross income like other self-employed professionals.<sup>189</sup> Thus, although art owners and artists cannot pay their income taxes directly with art, donating or creating artwork may indirectly produce substantial deductions.

#### A. Reducing Income Taxes Through Charitable Donations

Both individuals and corporate entities may receive a tax deduction for charitable contributions—made either in the form of money or property—to reduce their taxable income under I.R.C. § 170.<sup>190</sup> This Section, however, will focus narrowly on the tax consequences of an individual's donation of artwork to a charity. In general, by donating art to a charitable institution, a taxpayer may claim a deduction from his adjusted gross income.<sup>191</sup> According to the circumstances surrounding the donation, the deduction is based on either (1) the full fair market value or (2) the basis of the art.<sup>192</sup> However, in either case, the precise amount a taxpayer can deduct is capped at a certain percentage of the taxpayer's "contribution base."<sup>193</sup> As a rule, a taxpayer may not deduct more than fifty percent of his contribution base for all charitable donations to public charities in a given tax year, but a deduction claimed for a specific

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<sup>188</sup> See *infra* Section III.A.

<sup>189</sup> See *infra* Section III.B.

<sup>190</sup> I.R.C. § 170(b)(1)–(2). Interestingly, the United Kingdom studied the United States' treatment of charitable donations in crafting CGS. See ARTS COUNCIL ENG., ACCEPTANCE IN LIEU: REPORT 2010–2012, at 6 (2012), [http://www.artscouncil.org.uk/media/uploads/pdf/Acceptance\\_In\\_Lieu.pdf](http://www.artscouncil.org.uk/media/uploads/pdf/Acceptance_In_Lieu.pdf) [<https://perma.cc/6ZL7-TUKY>] ("Lifetime gift schemes of this kind are highly successful in many European countries and in North America and are an effective way for museums and other institutions to enhance their collections.")

<sup>191</sup> Adjusted gross income is calculated by subtracting specified deductions from a taxpayer's gross income. See I.R.C. § 62(a) (listing all specified deductions, including business expenses, retirement savings, alimony payments, and others). Any deductions claimed under I.R.C. § 170 for charitable contributions are then subtracted from a taxpayer's adjusted gross income to reduce taxable income. *Id.* § 63(a).

<sup>192</sup> See Anne-Marie E. Rhodes, *Big Picture, Fine Print: The Intersection of Art and Tax*, 26 COLUM. J.L. & ARTS 179, 187–93 (2003) (explaining the factors involved in calculating the deduction and noting that the difference between a full fair market value or basis deduction can be significant).

<sup>193</sup> See *id.* at 189 ("There are two types of quantitative limitations for charitable transfers. The first is the general percentage limitation for all transfers made by the taxpayer to charities within that taxable year. The second quantitative limitation depends on distinctions between the type of property donated (capital gain property or ordinary income property) and the status of the donee charity as public or private." (footnotes omitted)). A "contribution base" is essentially adjusted gross income but disregarding "net operating loss carryback." I.R.C. § 170(b)(1)(G); 3 RALPH E. LERNER & JUDITH BRESLER, *ART LAW: THE GUIDE FOR COLLECTORS, INVESTORS, DEALERS AND ARTISTS* 1565–66 (3d ed. 2005).

donation of artwork may be capped at twenty or thirty percent instead.<sup>194</sup> If the art's full fair market value or basis is worth more than the applicable percentage limit allows, the taxpayer may claim the surplus as a deduction in the next five taxable years.<sup>195</sup>

Within this general scheme, if a taxpayer's art has appreciated in value since he acquired it, then receiving a deduction for the art's full fair market value would be desirable. However, a taxpayer cannot merely choose one type of income tax deduction over the other. Instead, the nature of the donation itself determines whether the taxpayer qualifies for a deduction based on the fair market value or the basis of the art and the applicable percentage limit. As such, to secure a full fair market value deduction, Ralph Lerner and Judith Bresler urge taxpayers to strategically consider four issues when donating art: (1) whether the organization receiving the art is a public or private charity; (2) whether the art qualifies as a long-term capital gain; (3) whether the use of the art is related to the receiving organization's charitable intent; and (4) whether a qualified appraiser has issued a qualified appraisal of the art.<sup>196</sup> For instance, if the charity is public, the art is capital gain property, the use is sufficiently related to the charity's purpose, and the taxpayer receives a qualified appraisal, then the deduction is based on the art's full fair market value and the percentage limit is capped at thirty percent of the taxpayer's contribution base.<sup>197</sup> The following provides a general overview of each of these requirements.

### 1. The Type of Charitable Organization

To gain a tax deduction under I.R.C. § 170, a taxpayer must donate the art to a charitable organization.<sup>198</sup> Such charities can be public or private, but this distinction has significant consequences: a taxpayer will receive a deduction for the art's full fair market value if he donates to a public charity, but will be restricted to a deduction for the art's basis if he donates to a private charity.<sup>199</sup> Dependent in part on public funds, public charities are manifold and comprise "churches, schools, hospitals, museums, and other publicly supported

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<sup>194</sup> A detailed discussion of the percentage limits is beyond the scope of this Comment; for a comprehensive overview and examples of how these limits apply to tax deductions for art, see Rhodes, *supra* note 192, at 189-90, and 3 LERNER & BRESLER, *supra* note 193, at 1565-68, 1714.

<sup>195</sup> See Rhodes, *supra* note 192, at 189-90 (explaining the circumstances in which a surplus may be applied in subsequent tax years and referring readers to I.R.C. § 170(b)(1)(B), (b)(1)(C)(ii), (b)(1)(D)(ii), (d)(1)(A)).

<sup>196</sup> 3 LERNER & BRESLER, *supra* note 193, at 1555.

<sup>197</sup> *Id.* at 1555, 1566; Rhodes, *supra* note 192, at 189-93. In such a case, a taxpayer with a contribution base of \$100,000 could deduct up to \$30,000 of the fair market value of the art and claim any surplus value as a deduction in the next five tax years.

<sup>198</sup> 3 LERNER & BRESLER, *supra* note 193, at 1555.

<sup>199</sup> *Id.* at 1556.

organizations; private operating foundations; and certain organizations operated in connection with another public organization.”<sup>200</sup> Private charities, on the other hand, are tax-exempt entities that depend on private resources.<sup>201</sup> Significantly, Lerner and Bresler warn that just because an organization has been granted exempt status under I.R.C. § 501(c)(3),<sup>202</sup> it does not necessarily qualify as a public charity for purposes of a charitable deduction.<sup>203</sup> Thus, a taxpayer seeking the more generous fair market value deduction should donate art to charities characterized as public.

## 2. The Nature of the Donated Property

To be eligible for a full fair market value deduction, the donated art must qualify as capital gain property as opposed to ordinary income property.<sup>204</sup> If the art is (1) a capital asset,<sup>205</sup> (2) has gained value, and (3) has been in the possession of the taxpayer for more than one year, it is considered capital gain property.<sup>206</sup> However, Lerner and Bresler caution that if the art was either fashioned by the taxpayer herself (that is, if an artist wishes to donate her own artwork), accepted as a gift directly from the artist, treated as part of an art dealer’s inventory, owned for only a year or less, or is capable of resulting in a loss upon its sale, then the art is treated as ordinary income property and cannot be deducted at its full fair market value.<sup>207</sup> Instead, the taxpayer’s tax deduction is reduced to the art’s basis.<sup>208</sup>

## 3. Satisfying the Related Use Rule

A charitable donation must also fulfill the “related use” rule to receive a deduction for the full fair market value of the art.<sup>209</sup> Essentially, this requires that the organization receiving the donation *use* the art in a manner related to

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<sup>200</sup> *Id.* at 1555 (citation omitted); *see also id.* (explaining that even private foundations that dispense all of their funds each year may be considered “public”); I.R.C. § 170(b)(1)(A)(i-viii) (listing public charities).

<sup>201</sup> 3 LERNER & BRESLER, *supra* note 193, at 1555.

<sup>202</sup> *See* I.R.C. § 501(c)(3) (listing tax-exempt organizations).

<sup>203</sup> *See* 3 LERNER & BRESLER, *supra* note 193, at 1556 (explaining that I.R.C. § 509(a) defines public charities).

<sup>204</sup> *Id.* at 1556-58.

<sup>205</sup> A “capital asset” is “property held by the taxpayer;” however, certain types of property do not qualify, such as “artistic compositions” created by a taxpayer. I.R.C. § 1221(a)(3).

<sup>206</sup> 3 LERNER & BRESLER, *supra* note 193, at 1556; *see also* I.R.C. § 170(b)(1)(C)(iv) (defining capital gain property as “any capital asset the sale of which at its fair market value at the time of the contribution would have resulted in gain which would have been long-term capital gain”).

<sup>207</sup> 3 LERNER & BRESLER, *supra* note 193, at 1558; *see also* I.R.C. § 1221(a).

<sup>208</sup> 3 LERNER & BRESLER, *supra* note 193, at 1558-59; Rhodes, *supra* note 192, at 189.

<sup>209</sup> 3 LERNER & BRESLER, *supra* note 193, at 1555.

the organization's purpose as shown in its tax-exempt 501 status.<sup>210</sup> The legislative history provides some examples of how this rule should be employed:

[A] clear case [of satisfying the related use rule] is a gift of a picture or work of sculpture . . . to a museum. [However,] . . . with respect to a college or university [there is a question] as to whether or not they are using this for their exempt purpose . . . [of] teaching. Of course, the college could have a course in art, and if the gift were to be used for that purpose it would probably qualify as such a gift.<sup>211</sup>

This inquiry is clearly factually driven. For example, the IRS has said that the donation of a porcelain collection to a nonprofit retirement center satisfied the related use test; it reasoned that the adornments were “functionally related to [the retirement center]’s principal activity of creating a living environment for . . . residents because the display of the porcelains directly enhances that environment.”<sup>212</sup> Nonetheless, it is unclear whether giving a valuable sculpture to a soup kitchen would also pass muster. Presumably, a soup kitchen’s principal activity is to feed the poor. Is providing an aesthetically pleasing dining experience sufficiently related to that purpose? As in the case of the retirement center, it may enhance the dining environment, but the outcome would hinge on the charity’s stated purpose as a tax-exempt entity.

#### 4. Receiving a Qualified Appraisal from a Qualified Appraiser

Finally, to secure a fair market value deduction for a charitable donation, Lerner and Bresler explain that the donated art must meet certain appraisal requirements.<sup>213</sup> Because of concerns that taxpayers will overstate the value of donated objects,<sup>214</sup> the IRS requires that taxpayers receive a qualified appraisal, submit an appraisal summary, and preserve records about the donation for any object that is valued at \$5000 or more to ensure that the

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<sup>210</sup> See *id.* at 1561-63 (explaining when a taxpayer may regard a donated object as satisfying the related use rule). If the receiving organization sells the art within three years of the donation, the taxpayer could lose the full fair market value deduction. I.R.C. § 170(e)(7). To protect the full fair market value deduction from recapture, a prudent taxpayer should obtain certification from the organization about the art’s intended use and how it was related to the organization’s purpose when the donation is made. *Id.*

<sup>211</sup> 115 CONG. REC. 40,869 (1969), reprinted in 3 LERNER & BRESLER, *supra* note 193, at 1563.

<sup>212</sup> I.R.S. Priv. Ltr. Rul. 81-43-029 (July 29, 1981); see also 3 LERNER & BRESLER, *supra* note 193, at 1564 (mentioning the porcelain collection donation and providing further examples of IRS Private Letter Rulings about what qualifies as a related use).

<sup>213</sup> See 3 LERNER & BRESLER, *supra* note 193, at 1514-19 (outlining the process for obtaining a qualified appraisal and filing Form 8283).

<sup>214</sup> See 2 DUBOFF ET AL., *supra* note 186, at N-37 (“The greatest problem with deductions of tangible property at fair market value has always been the temptation to overvalue.”).

deduction claimed is accurate.<sup>215</sup> The third-party appraisal is intended to confirm that the “amount of the contribution is the fair market value of the property at the time of the contribution.”<sup>216</sup>

Tax returns with charitable donations of art valued at \$50,000 or more are subject to additional scrutiny.<sup>217</sup> If the IRS audits a taxpayer’s tax return and sees an appraisal of a piece of art valued at \$50,000 or more, it must transfer the appraisal to the Art Appraisal Services unit, which may submit it to the Art Advisory Panel for review.<sup>218</sup> Established in 1968,<sup>219</sup> the Art Advisory Panel “helps [the] IRS review and evaluate property appraisals submitted by taxpayers in support of the fair market value claimed for works of art included in federal income, estate and gift tax cases.”<sup>220</sup> It is comprised of twenty-five distinguished art specialists who are not remunerated for their evaluations.<sup>221</sup> These panelists are expected to offer “information, advice, and insight into the world of art” and draw on their “personal experience as dealers, scholars, and museum curators, and from information obtained from other members of their relatively small industry” in assessing valuations.<sup>222</sup>

Once a tax return is referred to the Art Advisory Panel for review, the panelists must determine whether the taxpayer’s fair market valuation of the work in question is “clearly justified, questionable, or clearly unjustified” and make a recommendation to the Art Appraisal Services unit about whether the valuation should be increased or decreased.<sup>223</sup> Although such recommendations are advisory, the Art Appraisal Services unit and the IRS usually adopt the Art Advisory Panel’s stance.<sup>224</sup> For example, in 2014, the Art Appraisal Services unit “adopted in full 90% of the Panel’s recommendations and adopted the rest in part.”<sup>225</sup> Given the scrutiny with which deductions for art donations are reviewed, a taxpayer would be unwise to exaggerate the fair market value of donated artwork and should seek to work with honest qualified appraisers.

<sup>215</sup> 3 LERNER & BRESLER, *supra* note 193, at 1514-15; I.R.C. § 170(f)(11)(C).

<sup>216</sup> Treas. Reg. § 1.170A-1(c)(1) (2015).

<sup>217</sup> *Art Appraisal Services*, I.R.S., <http://www.irs.gov/Individuals/Art-Appraisal-Services> [<https://perma.cc/XMR9-NSPW>] (last updated July 29, 2015).

<sup>218</sup> THE ART ADVISORY PANEL OF THE COMM’R OF INTERNAL REVENUE, ANN. SUMMARY REP. FISCAL YEAR 2014, at 2 [hereinafter ART ADVISORY PANEL ANNUAL SUMMARY REPORT 2014], <http://www.irs.gov/pub/irs-utl/annrep2014.pdf> [<https://perma.cc/D5RG-4P4J>]; *Art Appraisal Services*, *supra* note 217.

<sup>219</sup> ART ADVISORY PANEL ANNUAL SUMMARY REPORT 2014, *supra* note 218, at 2; *see also* McCarthy, *supra* note 184, at 15 (explaining that abuses in tax return valuations led to the creation of the Art Advisory Panel).

<sup>220</sup> *Art Appraisal Services*, *supra* note 217.

<sup>221</sup> *Id.*

<sup>222</sup> ART ADVISORY PANEL ANNUAL SUMMARY REPORT 2014, *supra* note 218, at 2.

<sup>223</sup> 3 LERNER & BRESLER, *supra* note 193, at 1523.

<sup>224</sup> ART ADVISORY PANEL ANNUAL SUMMARY REPORT 2014, *supra* note 218, at 3.

<sup>225</sup> *Id.*

## 5. Observations

As Lerner and Bresler's guidelines demonstrate, earning an income tax deduction for a charitable donation of art involves strategy, but it also reveals a great deal about how the tax laws treat art. First, the IRC gives the taxpayer considerable discretion in choosing the art to be donated, selecting the receiving charity, and determining the value of the art. Second, the IRC does not place any restrictions on what type of art or cultural property is worthy of a tax deduction. Instead, the charitable organization has complete discretion over whether to accept the art or not, regardless of whether it is a famous masterpiece or a relatively unknown work. Thus, it is the charity's acceptance that ultimately triggers a claim for a tax deduction. Finally, the Art Advisory Panel will only assess the valuation of donated art if a piece of artwork is accepted, claimed as a tax deduction, and referred by the IRS. While the Art Advisory Panel's determinations cannot be a precise science, its discerning review process thwarts overstated valuations and promotes fairness and accuracy. Overall, although the IRC gives philanthropic art owners indirect income tax benefits, the procedures governing deductions for charitable donations have meaningful requirements and practical safeguards to uphold a tax system based largely on "voluntary compliance."<sup>226</sup>

### B. *Income Taxes for Artists*

#### 1. The Rationale for Identical Tax Treatment

The United States does not allow artists to pay income taxes with artwork. Instead, everyone—regardless of his profession—must pay in cash.<sup>227</sup> This identical treatment raises a threshold question of "whether or not the income of artists *should* . . . be treated differently to that of other taxpayers."<sup>228</sup> On the one hand, artists earn a living from their artistic work just like other employed or self-employed individuals; thus, from a revenue-raising perspective, any difference in tax treatment would be unfair and unjustified. On the other hand, the United States generally views art as a social good and already seeks to cultivate the arts through generous deductions for charitable donations.<sup>229</sup> The question is whether federal income tax policy should go further. Like Mexico, should the United States seek to accommodate artists and further their creative activity in a more *direct* manner?

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<sup>226</sup> *Id.* at 2.

<sup>227</sup> See *supra* notes 182–83 and accompanying text.

<sup>228</sup> John W. O'Hagan, *Tax Expenditures: Pervasive, 'Hidden' and Undesirable Subsidies to the Arts?*,

29 HOMO OECOMICUS 329, 340 (2012) (emphasis added).

<sup>229</sup> See *supra* Section III.A.

Thus far, the IRC and the tax courts have answered this question in the negative. This position likely stems from the view that an artist's earnings from the sale of her artwork qualify as ordinary income,<sup>230</sup> but it also simply appears more equitable. In *Tobey v. Commissioner*, for example, the court likened an artist's earnings to that of other taxpaying professionals, observing,

For the most part, the present-day artist is a hard-working, trained, career-oriented individual. His education, whether acquired formally or through personal practice, growth, and experience, is often costly and exacting. He has keen competition from many other artists who must create and sell their works to survive. To avoid discriminatory treatment, we perceive no sound reasons for treating income earned by the personal efforts, skill, and creativity of a Tobey or a Picasso any differently from the income earned by a confidence man, a brain surgeon, a movie star or, for that matter, a tax attorney.<sup>231</sup>

Thus, unlike Mexico, which avoids burdening artists' creative activity<sup>232</sup> and accommodates their unique earning patterns through *Pago en Especie*,<sup>233</sup> the United States does not favor artists' endeavors—however noble—above those of other taxpayers. The federal taxman is blind as to profession.<sup>234</sup>

## 2. Tax Deduction Disadvantages

When it comes to the deduction rules however, the IRC arguably disadvantages artists in two ways and casts doubt on the principle of identical treatment. First, if an artist donates her own artwork to a charitable organization, she may not receive a deduction for the fair market value of the work.<sup>235</sup> Instead, she can only receive a tax deduction for the cost of the materials used to make that particular work, which may be negligible.<sup>236</sup> Many artists believe this is profoundly inequitable considering that art collectors may donate their

<sup>230</sup> See I.R.C. § 1221(a)(3)(A) (2012) (excluding an artist's own artwork from qualifying as a capital asset); 2 DUBOFF ET AL., *supra* note 186, at O-1 (“[A]n artist's work has been characterized primarily as ordinary income property.”).

<sup>231</sup> 60 T.C. 227, 235 (1973). Although the *Tobey* court refused to disadvantage artists relative to other taxpayers, this language also suggests that it would neither discriminate in their favor.

<sup>232</sup> See Crespo de la Serna, *supra* note 36 (praising *Pago en Especie* for not distracting artists with taxes when they are searching for creative inspiration).

<sup>233</sup> See Melián, *supra* note 104 (discussing artists' unpredictable cash flows).

<sup>234</sup> See 2 DUBOFF ET AL., *supra* note 186, at O-1 (“Artists rarely think of themselves as being engaged in business. In fact, many go to great lengths to avoid what they consider to be commercialism. Although artists' earning patterns and characteristics are often very unlike those of other businesspeople, the tax laws do not address these unique concerns.”).

<sup>235</sup> *Id.* at N-29, O-23; see also I.R.C. § 1221(a)(3) (excluding any “artistic composition” that is held by “a taxpayer whose personal efforts created such property” from qualifying as a capital asset, meaning that it cannot be considered capital gain property and secure a fair market value deduction).

<sup>236</sup> 2 DUBOFF ET AL., *supra* note 186, at N-29, O-23.



works and receive a full fair market value deduction; however, this statutory prohibition applies not only to artwork, but also to “IBM’s computers, to a lawyer’s brief, . . . [and] to a cabinet-maker’s table.”<sup>237</sup> Thus, artists are treated no differently than creators of other goods under the tax deduction rules, although they are disadvantaged relative to art collectors.<sup>238</sup>

Second, many artists believe the deduction rules make it difficult to successfully deduct their business expenses. Like other self-employed professionals who engage in an activity for the purpose of making a profit,<sup>239</sup> artists may deduct business expenses accumulated in the course of their creative expression.<sup>240</sup> For an artist, such deductions can be significant because they can include the cost of materials (for example, canvas, paint brushes, or clay), fees for renting a gallery or studio, and even tuition expenses for further education.<sup>241</sup> Nevertheless, determining who qualifies as a profit-seeking artist—as opposed to a hobbyist—can be very challenging. For instance, “no one would suggest disallowing the expenses in starting a carpet-cleaning business as hobby-related, nor allowing deduction of equipment for backpacking. [However, t]he fundamental problem is that artists do for a living what many people do for fun.”<sup>242</sup> This inquiry becomes especially murky when an artist finds it necessary to hold another job to support herself.<sup>243</sup> Can a part-time artist deduct her art expenses? Deciding who may deduct business expenses for artistic endeavors is not always straightforward.

An early case that addressed the issue of who qualifies as a profit-seeking artist was *Churchman v. Commissioner*.<sup>244</sup> In that case, Gloria Churchman had worked as an artist for twenty years.<sup>245</sup> While she was primarily a painter, her other artistic endeavors included sculpting, designing, drawing, writing, acting, and making a film.<sup>246</sup> However, throughout the period in question, she

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<sup>237</sup> See JOHN HENRY MERRYMAN & ALBERT E. ELSEEN, LAW, ETHICS, AND THE VISUAL ARTS 811 (4th ed. 2002) (critiquing artists’ claims that certain tax reforms unfairly burden them more than other creators).

<sup>238</sup> *Id.*

<sup>239</sup> See 26 Treas. Reg. § 1.183-2(a) (1972) (“Except as provided in section 183 and § 1.183.1, no deductions are allowable for expenses incurred in connection with activities which are not engaged in for profit. Thus, for example, deductions are not allowable under section 162 or 212 for activities which are carried on primarily as a sport, hobby, or for recreation.”).

<sup>240</sup> See 26 I.R.C. § 162(a) (allowing for the deduction of salaries or compensation for services, meals and lodging during travel, and rentals for business purposes).

<sup>241</sup> For a description of the types of business expenses incurred by artists, see FELD ET AL., *supra* note 185, at 16-17 (1983) and MERRYMAN & ELSEEN, *supra* note 237, at 797.

<sup>242</sup> FELD ET AL., *supra* note 185, at 17.

<sup>243</sup> *Id.*

<sup>244</sup> 68 T.C. 696 (1977).

<sup>245</sup> *Id.* at 697.

<sup>246</sup> *Id.*

never financially profited from her work.<sup>247</sup> When she and her husband submitted a series of tax returns claiming deductions for an in-house studio and various artistic activities, the IRS denied those deductions, finding that she was not an artist.<sup>248</sup> In considering the record, the Tax Court noted that certain factors supported Churchman's lack of a profit motive, including that Churchman had never depended on the income from her art and that there was an "inherent" recreational element in her artistic endeavors.<sup>249</sup> However, the court viewed these factors contextually, reasoning that "such a history of losses is *less persuasive in the art field than it might be in other fields* because the archetypal 'struggling artist' must first achieve public acclaim before her serious work will command a price sufficient to provide her with a profit."<sup>250</sup> That said, the court also considered Churchman's other activities: She opened and directed an art gallery for a year, organized a mailing list, solicited galleries to exhibit her work, published a book, and kept receipts of all of her art expenses and sales.<sup>251</sup> She had also studied art, taught art, published articles, exhibited work in commercial galleries, sold work, and received a grant to produce a film.<sup>252</sup> Overall, the court found that her artistic activities qualified as a for-profit enterprise and that—as an artist—Churchman could legitimately deduct her artistic expenses from her income taxes.<sup>253</sup>

In October 2014, the Tax Court revisited the question of who qualifies as an artist in *Crile v. Commissioner*.<sup>254</sup> In that case, Susan Crile had worked for over forty years as an artist in various media but was also a tenured professor of studio art at Hunter College.<sup>255</sup> The IRS challenged her deductions of artistic business expenses, claiming that the separation of her artistic and teaching careers was artificial; for tax purposes, it insisted, she was a teacher.<sup>256</sup> Under the deduction rules for business expenses, Crile had to "show that she engaged in the activity with an actual and honest objective of making a profit" in order to receive the deductions.<sup>257</sup> To determine whether Crile intended to earn a profit from her artistic activities, the court used the nine-factor test outlined in the regulations, which examines the following:

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<sup>247</sup> *Id.* at 699.

<sup>248</sup> *Id.*

<sup>249</sup> *Id.* at 701.

<sup>250</sup> *Id.* at 701-02 (emphasis added).

<sup>251</sup> *Id.* at 702.

<sup>252</sup> *Id.*

<sup>253</sup> *Id.* at 703.

<sup>254</sup> 108 T.C.M (CCH) 372 (2014).

<sup>255</sup> *Id.* at 373.

<sup>256</sup> *Id.* at 378.

<sup>257</sup> *Id.* at 377.

(1) the manner in which the taxpayer conducts the activity; (2) the expertise of the taxpayer or her advisers; (3) the time and effort spent by the taxpayer in carrying on the activity; (4) the expectation that assets used in the activity may appreciate in value; (5) the success of the taxpayer in carrying on other similar or dissimilar activities; (6) the taxpayer's history of income or losses with respect to the activity; (7) the amount of occasional profits, if any; (8) the financial status of the taxpayer; and (9) elements of personal pleasure or recreation.<sup>258</sup>

Relying heavily on *Churchman* throughout its nine-factor analysis, the court found that the first, second, third, and fourth factors strongly favored Crile's assertion that she expected to profit from her artwork; the fifth, eighth, and ninth factors slightly favored her or were neutral; and the sixth and seventh factors favored the IRS.<sup>259</sup> Considering the factors overall, the court found that Crile had "an actual and honest expectation of making a profit"<sup>260</sup> and therefore held that her artistic and teaching careers should be treated separately for tax purposes.<sup>261</sup>

Reflecting on the significance of this case, Crile's lawyer Micaela McMurrugh said, "[A]rt is not a business like other businesses. And I think that's what this decision reflects."<sup>262</sup> Perhaps this is an early indication that artists will be increasingly distinguished from other professions in the tax laws. For now, however, artists remain subject to the same taxes as other taxpayers, but they may occasionally have to assert proof of their artistic careers for the IRS to recognize their business expense deductions, as demonstrated in *Churchman* and *Crile*.

#### IV. AN APPRAISAL OF *PAGO EN ESPECIE* AND THE CULTURAL GIFTS SCHEME INDICATES THAT THE UNITED STATES SHOULD NOT ADOPT A PAYMENT-IN-KIND INCOME TAX SCHEME

The celebration of *Pago en Especie*'s fiftieth anniversary in 2007 and the implementation of CGS in 2013 have increased public interest in payment-in-kind income tax schemes for art and cultural property. In a recent radio interview, Julián Zugazagoitia, the Director of El Museo del Barrio in New York City, praised *Pago en Especie* for fostering "great respect for . . . artists and an admiration for what they bring to the cultural heritage [of Mexico]."<sup>263</sup>

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<sup>258</sup> *Id.* at 378-79.

<sup>259</sup> *Id.* at 384.

<sup>260</sup> *Id.*

<sup>261</sup> *Id.*

<sup>262</sup> Randy Kennedy, *Tax Court Ruling Is Seen as a Victory for Artists*, N.Y. TIMES (Oct. 6, 2014), <http://www.nytimes.com/2014/10/07/arts/design/tax-court-ruling-is-seen-as-a-victory-for-artists.html> [<https://perma.cc/KW2N-8ZF8>].

<sup>263</sup> *In Mexico, Artists Pay Taxes with Paintings*, *supra* note 19.

When asked whether there was a movement to adopt such a payment-in-kind program in the United States, Zugazagoitia responded affirmatively:

[T]he Association of Art Museum Directors . . . ha[s] been trying to talk to our legislators in the United States to make that possible . . . . The U.S. has always been in [sic] the forefront of philanthropy but for once Mexico has a very good example that I think would be interesting to replicate here.<sup>264</sup>

Zugazagoitia is not alone. A *Forbes* article, titled *Paying Tax with Art is Legal in UK & Mexico, Why Not in US?*, recently asked the same question.<sup>265</sup>

It is indisputable that *Pago en Especie* and CGS have obtained valuable works for the edification of future generations in their respective countries.<sup>266</sup> For Mexico in particular, *Pago en Especie* has amassed an enviable collection of contemporary artwork.<sup>267</sup> However, proponents of these programs seem to take for granted that a government *should* be directly involved in building a national art collection and enriching the cultural landscape. The thrill of accumulating a vast trove of art seems to have obfuscated any attempts to objectively scrutinize these two payment-in-kind programs. When considered from a policy perspective, there are several reasons to be skeptical about adopting such a program in the United States, including (1) the loss of tax revenue in a direct and partial manner; (2) the commitment of future public funds for the conservation, storage, and exhibition of the art; (3) the preferential treatment of state-run museums over private museums; (4) the difficulty of determining what art should qualify; (5) the possibility that others will demand similar treatment; and (6) the danger of introducing subjectivity and preferential treatment in a tax system where the appearance of fairness, objectivity, and precision is important.

#### A. *Payment-in-Kind Programs Forgo Large Sums of Tax Revenue in a Direct and Selective Manner*

In order to accept works of art and cultural property under *Pago en Especie* and CGS, Mexico and the United Kingdom have and will continue to forfeit significant sums of money in exchange for artistic objects. Is this tradeoff

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<sup>264</sup> *Id.*

<sup>265</sup> Wood, *supra* note 19.

<sup>266</sup> *See, e.g.*, Decree of 1975, *supra* note 56 (supporting the collection and public exhibition of *Pago en Especie* works because they are “an example of the national artistic creation of our time”); Press Release, Dep’t for Culture, Media & Sport, Museums and Galleries Set to Benefit from New “Lifetime Giving” Incentive (March 12, 2013), <https://www.gov.uk/government/news/museums-and-galleries-set-to-benefit-from-new-lifetime-giving-incentive> [<https://perma.cc/5MBD-R2P6>] (quoting Culture Minister Ed Vaizey as saying, “This new scheme is aimed at encouraging gifts and donations of wonderful treasures to the nation, where they can be enjoyed by all”).

<sup>267</sup> *See, e.g.*, Hershaw, *supra* note 13 (noting that *Pago en Especie* has collected over 7000 works).

worth it? In her recent article on *Pago en Especie*, Eva Hershaw reported that Mexico has *never* estimated the value of the *Pago en Especie* collection; likewise, it has “never calculated the tax revenue lost to . . . *Pago en Especie*.”<sup>268</sup> Indeed, the only figure the government tracks is the number of works it has received through the program.<sup>269</sup> As a result of such opaque recordkeeping, Hershaw observed that it is very difficult to make an “economic argument calling for [*Pago en Especie*’s] abolishment.”<sup>270</sup> Instead, the program is effectively insulated from economic criticism. Of course, some view *Pago en Especie*’s forfeited revenue as a sunk cost, predicting that artists would not pay their taxes at all if forced to pay in cash, so nothing is lost.<sup>271</sup> However, such an assertion is completely groundless. Irregular cash flows may make income taxes burdensome for artists,<sup>272</sup> but it does not preclude them from paying in cash. Moreover, a creative tax system that allows artists to pay in cash every two or three years could effectively accommodate their irregular cash patterns.

While it is hard to criticize *Pago en Especie* without knowing the exact amount of forgone revenue, it is safe to assume that the numbers are significant: over a sixty-year period, the SHCP has collected almost 7000 works.<sup>273</sup> Choosing to forfeit revenue is not a trivial decision, especially considering that between 1970 and 2010, money laundering, tax evasion, and corruption have cost Mexico \$872 billion.<sup>274</sup> As a country “with one of the largest gaps between rich and poor,” this is “an enormously damaging drainage of resources” because it is “money that could have been used to invest in education, to build roads or to fight drug cartels.”<sup>275</sup> To exacerbate the problem, Mexico has a very poor history of collecting taxes<sup>276</sup> and has lower income tax rates compared to other countries.<sup>277</sup> These difficulties have continued in recent years:

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<sup>268</sup> *Id.*

<sup>269</sup> *Id.*

<sup>270</sup> *Id.*

<sup>271</sup> *See id.* (quoting a lawyer as saying, “The truth is, before, most artists simply didn’t pay their taxes”).

<sup>272</sup> *See supra* Section I.D.

<sup>273</sup> Hershaw, *supra* note 13.

<sup>274</sup> *Id.* (citing Tracy Wilkinson, *Money Laundering, Tax Evasion Suck Billions from Mexican Economy*, L.A. TIMES: WORLD NOW (Jan. 30, 2012), [http://latimesblogs.latimes.com/world\\_now/2012/01/money-laundering-tax-evasion-suck-billions-from-mexican-economy-study.html](http://latimesblogs.latimes.com/world_now/2012/01/money-laundering-tax-evasion-suck-billions-from-mexican-economy-study.html) [<https://perma.cc/7FRT-FZEF>]).

<sup>275</sup> *See* Wilkinson, *supra* note 274 (quoting remarks made by Raymond W. Baker, director of Global Financial Integrity, at a news conference in 2012).

<sup>276</sup> *See* Claudio Lomnitz, *Three Causes Behind Mexico’s Crisis of Corruption and Impunity*, HUFFINGTON POST: WORLD POST (Nov. 19, 2014, 5:47 PM), [http://www.huffingtonpost.com/claudiolomnitz/mexico-corruption-causes\\_b\\_6186682.html](http://www.huffingtonpost.com/claudiolomnitz/mexico-corruption-causes_b_6186682.html) [<https://perma.cc/NMR5-DVXQ>] (explaining that Mexico’s history of collecting low levels of tax revenue is due to its dependence on its state-run oil company for revenue).

<sup>277</sup> *See* Ben Carter, *Which Country Has the Highest Tax Rate?*, BBC NEWS (Feb. 25, 2014), <http://www.bbc.com/news/magazine-26327114> [<https://perma.cc/P33K-X5CT>] (explaining that Mexico’s

Mexico's tax revenues as a percent of GDP are the lowest among the OECD countries at around 10 percent. About half of Mexico's population lives in poverty and thus pay [sic] no taxes. Of the other half, 60 percent are estimated to be in the informal sector[,], which means they pay little or no taxes. So the burden of taxation rests with 20 percent of Mexicans.<sup>278</sup>

Within this context, exempting all artists from paying income taxes takes on a graver meaning.

Despite pressure from the International Monetary Fund (IMF), there is no sign that Mexico will retire *Pago en Especie* to increase its income tax revenue.<sup>279</sup> Instead, the government has heightened its scrutiny of corporations that have evaded taxes<sup>280</sup> and increased taxes on businesses that already pay.<sup>281</sup> Those running *Pago en Especie* are not concerned about the IMF because there is "a social benefit to programs like this one that doesn't easily fit into the IMF's matrices."<sup>282</sup> Moreover, *Pago en Especie* enjoys widespread support.<sup>283</sup> Nonetheless, if the IMF continues to pressure Mexico for more transparency and accountability in collecting taxes, *Pago en Especie* may eventually have to calculate the amount of revenue forgone by accepting artwork. Alternatively, it may have to value the works it holds in its collections to provide a more robust justification for the program. Either result would be positive since it would enable policymakers to better evaluate *Pago en Especie*'s advantages and disadvantages.

In the United Kingdom, the picture is slightly different. The consequences of forgoing tax revenue may not drastically affect infrastructure or education, but programs like CGS still involve significant amounts of money. For example, from 2004 to 2014, CGS and AIL wrote off £167.8 million in taxes.<sup>284</sup> With the 2014 budget increase, in 2015 CGS and AIL together will

9.5% income tax rate for a single person with no children on an average salary and for a married couple with two children on an average salary is one of the lowest rates among OECD countries).

<sup>278</sup> James R. Jones et al., *How Important Are Mexico's Proposed Tax System Reforms?*, INTER-AM. DIALOGUE (Sept. 18, 2013), <http://archive.thedialogue.org/page.cfm?pageID=32&pubID=3386&s=mexico%27s%20tax> [<https://perma.cc/B6UK-9JN5>]; see also *Fiscal Reform in Mexico: It's a Dog's Life*, ECONOMIST (Sept. 14, 2013), <http://www.economist.com/news/americas/21586337-tax-plan-dictated-politics-its-dogs-life> [<https://perma.cc/8RTF-TMC7>] (noting that sixty percent of the working population pays no taxes).

<sup>279</sup> Hershaw, *supra* note 13.

<sup>280</sup> *Id.*

<sup>281</sup> See Gabriel Stargardter, *Mexico Business Lobby Launches Legal Fight Against Tax Reform*, REUTERS (Feb. 12, 2014, 10:02 PM), <http://www.reuters.com/article/2014/02/13/mexico-reforms-idUSL2NoLl01420140213> [<https://perma.cc/ARP4-VMYG>] ("Critics . . . [claim that the tax reforms have] forced higher taxes on those already paying, instead of going after the millions outside the tax system.").

<sup>282</sup> Hershaw, *supra* note 13.

<sup>283</sup> See *id.* (quoting a *Pago en Especie* administrator as saying, "Everyone loves this program. We have no reason to think any of this is at risk").

<sup>284</sup> See CGS & AIL: REPORT 2014, *supra* note 18, at 5 (providing a table of the tax amount settled from 2004–2014).

be able to bestow tax reductions of up to £40 million a year in exchange for preeminent works.<sup>285</sup> Considering that the Treasury was owed more than £35 billion in outstanding taxes at the close of 2013,<sup>286</sup> it is unclear whether implementing programs to write off future tax revenue is the best course. Under these circumstances, at least the £40 million annual budget for CGS and AIL caps the amount of tax forgone, but one can still question whether the government ought to receive assets other than cash, especially when those assets are transferred *free of charge* to other institutions.

Of course, the United States—even without a payment-in-kind scheme—also forgoes revenue by allowing taxpayers to receive tax deductions for charitable donations of art.<sup>287</sup> In 2012 for example, taxpayers claimed income tax deductions for 144,090 charitable donations of art and collectibles worth over \$1.18 billion.<sup>288</sup> The decision to write off tax revenue reflects the competing purposes of tax laws in general: to collect revenue *and* patronize programs that serve social goods.<sup>289</sup> Mexico, the United Kingdom, and the United States seem to be in agreement that furthering the arts is one of these goods. However, the differences in how their respective tax systems accomplish this goal have profound implications.

In the United States, the federal tax laws further the arts by two methods: “[F]irst, taxes are collected and monies distributed in order to directly foster values that society considers important; and second, private investment is encouraged through tax advantages in those areas deemed socially worthwhile.”<sup>290</sup> Tax deductions for charitable donations fit within the latter category, and thus patronize the arts indirectly. Unlike Mexico, which directly assists artists, and unlike the United Kingdom, which directly benefits select owners of preeminent objects and the institutions that receive them, the United States does not accord *direct* special treatment to a distinct class of taxpayers. Instead, any taxpayer who chooses to make a charitable donation of artwork and fulfills all of the attendant conditions may subsequently apply for a tax deduction. Although the amount of the deduction permitted will vary,<sup>291</sup> the United States impartially offers these deductions to all taxpayers to support the arts in a less direct manner.

<sup>285</sup> *Id.* at 5; *Good News*, *supra* note 135.

<sup>286</sup> *Government Accepts Works of Art in Lieu of £125 Million in Tax Payments*, *supra* note 118.

<sup>287</sup> See *supra* Section III.A (discussing tax deductions for charitable donations).

<sup>288</sup> PEARSON LIDDELL & JANETTE WILSON, INTERNAL REVENUE SERV., STATISTICS OF INCOME: INDIVIDUAL NONCASH CONTRIBUTIONS, 2012, at 1 & fig.A (Spring 2015), <https://www.irs.gov/pub/irs-soi/soi-a-innc-id1507.pdf> [<https://perma.cc/A4ST-6EM4>] (compiling data from individual returns that used Form 8283 (Noncash Charitable Contributions), which must be used “when the amount of taxpayer deductions for all noncash donations on Schedule A, *Itemized Deductions*, exceeds \$500”).

<sup>289</sup> McCarthy, *supra* note 184, at 2.

<sup>290</sup> *Id.*

<sup>291</sup> See *supra* Part III (explaining the factors involved in determining the deducted amount and the restrictions that apply to artists).

Despite this, some might argue that the United States should adopt a strict cap for the amount of income tax written off (as in the United Kingdom) for art donations. There are two problems with this suggestion. First, if the United States were to instate a strict limit, it would have to determine which of the various art donations to recognize, since the cap would prevent it from recognizing all of them. This change would involve a great deal of government oversight and subjective decisionmaking. Second, the government may have to compensate for this cap by giving more tax revenue directly to artistic institutions so that they continue to flourish. Again however, selecting the institutions worthy of public support would require administrative supervision and subjective decisions. For these reasons, the United States should eschew a ceiling on forgone tax revenue from art donations; instead, it should preserve its indirect patronage of the arts by allowing taxpayers to deduct a certain percentage of their adjusted gross income for supporting the arts privately. While large sums of tax revenue are indeed at stake, the United States' method of forgoing this money indirectly and impartially is superior both to Mexico's direct method of exempting artists from paying in cash and to the United Kingdom's selective method of writing off taxes for owners of preeminent items.

B. *Payment-in-Kind Programs Commit Public Funds  
to the Custodial Care of Accepted Artwork*

Although Mexican artists express great pride in knowing that their work has become part of *Pago En Especie*,<sup>292</sup> there are surprisingly few discussions about how much money the SHCP spends to manage the ever-growing collection. Although the SHCP has created an "exhaustive catalogue where it specifies the characteristics of the works, their location, and exhibition history"<sup>293</sup> and continues to publish exquisite books about the accepted artwork,<sup>294</sup> none of these publications explain how *Pago en Especie* employs public funds to care for the works. Instead, they are conspicuously silent regarding the program's economic design and consequences.

Storage space and conservation efforts are two inescapable costs of a collection of almost 7000 works. Recently, the SHCP "has been forced to

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<sup>292</sup> See, e.g., Hershaw, *supra* note 13 (quoting an artist as saying, "[I]t is . . . a source of pride, knowing that your art will become part of a historic collection that reflects Mexico's creative heritage").

<sup>293</sup> Ganado Kim, *supra* note 2, at xii.

<sup>294</sup> See generally CATÁLOGO COLECCIÓN *PAGO EN ESPECIE* DE LA SECRETARÍA DE HACIENDA Y CRÉDITO PÚBLICO: 1987-1989 (1993) (documenting the works recently accepted under *Pago en Especie* with colorful photographs in order to highlight "the diversity and the artistic and cultural wealth of [Mexico]"); GANAMOS TODOS, *supra* note 111, at 8 (presenting, through the coordination of the SHCP and the Museo de Arte Contemporáneo de Monterrey, a selection of works from *Pago en Especie* that reveal "the vitality of Mexican society and its culture[,] . . . the imprint of diverse artistic trends, and the personal expression of each artist").



purchase additional warehouses in Mexico City to store an ever-growing collection of paintings, graphics, and sculptures.”<sup>295</sup> Moreover, because contemporary artists “experiment” greatly with different materials and methods, conservation needs and costs vary significantly.<sup>296</sup> For example, the costs of preserving, storing, and displaying a large painting<sup>297</sup> will likely be very different than those associated with a polystyrene sculpture that incorporates human hair.<sup>298</sup> While it is not clear how much the government spends to store, archive, conserve, research, transport, and exhibit the collection, the lack of transparency is concerning because, as a national collection, public funds must support it. Ultimately, although its purposes may be noble, without openly addressing these economic questions, *Pago en Especie* may soon face additional inquiries and harsher criticism.

In the United Kingdom, CGS does not raise as many concerns. Instead of assuming the financial responsibility for all CGS works, the government Minister merely facilitates the transfer of the work to an eligible institution. The receiving institution then assumes all of the costs of caring for the items: it must, “at its own expense, maintain the object in its existing condition and make good any repairable damage.”<sup>299</sup> Additionally, the institution must exhibit the object for the public’s benefit and may not transfer or sell the object without the Minister’s permission.<sup>300</sup> If the institution cannot meet these requirements, then it must inform the AIL Panel, which will offer advice about transferring the object to another institution.<sup>301</sup> Initially, CGS appears to avoid the problem of using public funds to care for accepted objects; however, since eligible institutions include public museums and galleries, it is likely that some public funding will ultimately be used to store, preserve, and exhibit CGS objects.<sup>302</sup>

For the United States, committing taxpayer funds to the care and conservation of art poses problems. The government already supports the arts by giving federal funds directly to institutions and programs like the

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<sup>295</sup> Hershaw, *supra* note 13.

<sup>296</sup> See MacMasters, *supra* note 11 (discussing how the use of different techniques can be a “challenge for conservation”).

<sup>297</sup> Rivera’s *Estudio del Artista*, for example, is quite large. See Sobrino Figueroa, *supra* note 8, at 35 (providing a photo of the painting that illustrates its great size).

<sup>298</sup> See MacMasters, *supra* note 11 (describing a sculpture called *Dentro del Ojo de Pesado* by Gerardo Azcúnaga).

<sup>299</sup> CGS: SCHEME & GUIDANCE 2015, *supra* note 136, para. 42(a).

<sup>300</sup> See *id.* paras. 42(b)-(c) (instructing institutions to exhibit objects for at least one hundred days per year, unless preservation needs require otherwise).

<sup>301</sup> *Id.* para. 42(d).

<sup>302</sup> See, e.g., *id.* paras. 4, 33 (identifying institutions eligible to receive CGS works); Elizabeth, *supra* note 168 (announcing the donation of a Van Gogh to the National Gallery, a public institution).

Smithsonian Museum,<sup>303</sup> but such funding is limited. If these organizations were to acquire a steady stream of art each year from a program like *Pago en Especie* or CGS, it is unclear how much additional funding they would require to care for a perpetually growing national collection. Accurate conservation estimates are difficult, if not impossible, to make because different objects require unique methods of preservation, storage, and display—all of which entail distinct costs. With the government already dependent on private funds to pay for significant cultural initiatives such as the restoration of the Washington Monument and the display of items in the National Archives,<sup>304</sup> it is unlikely that there would be enough public funding to commit to cataloging, archiving, preserving, storing, curating, and exhibiting a new national collection of artwork and cultural property.

C. *Payment-in-Kind Programs Favor State-Run Museums over Private Museums*

Both Mexico and the United Kingdom have many state-run museums, which may explain their preference for a payment-in-kind tax program.<sup>305</sup> Buying art on the open market is an expensive endeavor and, since state-run museums typically have a small budget for acquisitions, allowing them to collect art via a payment-in-kind system is advantageous.<sup>306</sup> In Mexico, where most museums are state-run, even large and prestigious art institutions can find themselves “cash-strapped.”<sup>307</sup> Moreover, Mexico simply does not have the United States’ history of private philanthropy to help museums augment their holdings or their budgets.<sup>308</sup> For example, Mexican fundraising groups comparable to the Metropolitan Museum of Art’s Curatorial Friends Groups or the Guggenheim’s Young Collectors Council are still in their infancy.<sup>309</sup> As such, *Pago en Especie* allows Mexico to enhance the collections of its state-run museums without having to compete on the open market for expensive new acquisitions.<sup>310</sup> If the development of fundraising groups causes state-run

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303 See *How Is the Smithsonian Institution Funded?*, SMITHSONIAN, <http://www.si.edu/giving/faqs> [<https://perma.cc/2QZ2-GW3Z>] (last visited Jan. 23, 2016) (“Federal appropriations cover about 70 cents of every dollar needed by the Smithsonian.”).

304 See Michael E. Ruane, *Billionaire Philanthropist Rubenstein to Give Millions to Help Fix Washington Monument*, WASH. POST (Jan. 18, 2012), [https://www.washingtonpost.com/local/billionaire-philanthropist-rubenstein-to-give-millions-to-help-fix-washington-monument/2012/01/18/gIQA PYmb9P\\_story.html](https://www.washingtonpost.com/local/billionaire-philanthropist-rubenstein-to-give-millions-to-help-fix-washington-monument/2012/01/18/gIQA PYmb9P_story.html) [<https://perma.cc/9JPE-WSHD>] (describing how David M. Rubenstein has entered into several “public-private partnerships” with the government to secure our “national icons”).

305 Glassman, *supra* note 181; Melián, *supra* note 104.

306 See Melián, *supra* note 104 (explaining that Mexico and many other Latin American countries have relatively small culture budgets for their state-run museums).

307 *Id.*

308 *Id.*

309 *Id.*

310 *Id.*

museums to be less dependent on *Pago en Especie* for acquisitions, or if more private museums emerge and challenge the advantages *Pago en Especie* affords state-run museums, then perhaps *Pago en Especie* will encounter more criticism; in the meantime, however, the program remains a cost-efficient way for Mexico to supplement the small budgets of its state-run museums.

In the United Kingdom, both public museums and other eligible institutions can receive CGS objects.<sup>311</sup> “In an era in which resources are stretched, but which is nonetheless an era of great public popularity for the arts,” eligible institutions obtain valuable CGS acquisitions without spending a pound.<sup>312</sup> In contrast, institutions that do not qualify for CGS—either because they are not public or because they do not provide sufficient public access to their collections<sup>313</sup>—must buy new acquisitions at fair market prices. As CGS becomes further established,<sup>314</sup> it will be interesting to see how these latter institutions fare in the competition for future acquisitions. Considering that institutions eligible for CGS can increase their collections without worrying about their budgets and can attract acquisitions with the promise of a tax reduction, institutions excluded from the payment-in-kind program will likely face challenges in building their collections.

If a payment-in-kind system were introduced to fulfill income tax obligations in the United States, it could adversely affect the United States’ private art museums and art collectors. Historically, private collectors have been both entrepreneurial in amassing collections and visionary in identifying new artistic talent.<sup>315</sup> As a result, private museums and collections “dominate the American art museum scene today.”<sup>316</sup> However, if taxpayers could extinguish their taxes entirely or receive a significant tax credit by giving artwork to federal museums, why would they even consider donating to a private museum for a

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311 CGS: SCHEME AND GUIDANCE 2015, *supra* note 136, paras. 4, 33.

312 See ARTS COUNCIL ENG., CULTURAL GIFTS SCHEME & ACCEPTANCE IN LIEU: REPORT 2015, at 4 (2015) [hereinafter CGS & AIL: REPORT 2015], [http://www.artscouncil.org.uk/media/uploads/Cultural\\_Gifts\\_Scheme\\_and\\_acceptance\\_in\\_lieu\\_report\\_2015.pdf](http://www.artscouncil.org.uk/media/uploads/Cultural_Gifts_Scheme_and_acceptance_in_lieu_report_2015.pdf) [https://perma.cc/XSZ2-AKA3]; see also *supra* Section II.D.

313 CGS: SCHEME AND GUIDANCE 2015, *supra* note 136, paras. 4, 33, 35(c), 42(b).

314 CGS & AIL: REPORT 2014, *supra* note 18, at 4 (noting that 2014 was the program’s “first full year of operation”).

315 See, e.g., MERRYMAN & ELSEN, *supra* note 237, at 1041 (noting that the J. Paul Getty Museum and the Norton Simon Museum are powerful examples of how private individuals have shaped the museum landscape); see also Jonathan Scott Goldman, *Just What the Doctor Ordered? The Doctrine of Deviation, the Case of Doctor Barnes’s Trust and the Future Location of the Barnes Foundation*, 39 REAL PROP. PROB. & TR. J. 711, 717 n.33 (2005) (“When Dr. Barnes began collecting art, many of the pieces that he bought were truly on the cutting edge of art and then-contemporary culture. People thought these images were uncivilized and grotesque; some challenged whether these images . . . even qualified as art at all. While artists such as Cézanne, Soutine, Seurat, and De Chirico now form the foundation of the socially acceptable and mainstream cannon [sic] of modern art history, this was far from the case when Dr. Barnes began his collection.”).

316 MERRYMAN & ELSEN, *supra* note 237, at 1041.

mere tax deduction? A federal payment-in-kind income tax system would almost certainly “give the National Gallery an advantage over the Metropolitan Museum and the Museum of Modern Art in the competition for great collections.”<sup>317</sup> This trend could severely alter the art landscape in the United States and lead to the impoverishment of private collections. Thus, unless the United States wishes to cast off its history of private philanthropy and disadvantage private museums from acquiring new works through charitable donations, it should not adopt a payment-in-kind program.

#### D. *Payment-in-Kind Programs Must Decide What and Who Is Worth Collecting*

A major challenge for all payment-in-kind tax schemes is determining *what kind of art* should be accepted. This problem is particularly acute for *Pago en Especie* because it only accepts art from living artists; thus, it is limited to contemporary art—a genre where the market price is not always readily apparent<sup>318</sup> and where the artistic media and methods frequently change.<sup>319</sup> For example, should the SHCP accept a pop art sculpture but deny an installation that is meant to disintegrate? Should a performance art piece qualify? If so, how would the SHCP “accept” it? Would a recording of the performance be sufficient? At one time, *Pago en Especie* accepted only paintings, graphics, and sculptures; now, it accepts more forms but still excludes industrial, artisanal, utilitarian, cinematic, applied, and architectural art.<sup>320</sup> It is very difficult to know where to draw the line since contemporary art, almost by definition, constantly pushes boundaries.

Like *Pago en Especie*, CGS also excludes certain kinds of cultural property. It will only accept a “picture, print, book, manuscript, work of art, scientific object or other thing that the relevant Minister is satisfied is pre-eminent for its national, scientific, historic or artistic interest.”<sup>321</sup> Thus, objects that are deemed less prestigious or significant will not qualify. While the Minister has

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<sup>317</sup> *Id.* at 1040-41. Although Merryman and Elsen raise this point with regard to the payment of estate taxes with art, it is an equally applicable and forceful argument to make when considering the consequences of paying income taxes with art.

<sup>318</sup> See generally DON THOMPSON, *THE SUPERMODEL AND THE BRILLO BOX: BACK STORIES AND PECULIAR ECONOMICS FROM THE WORLD OF CONTEMPORARY ART* (2014) (exploring the whims, motives, and economics behind prices in the contemporary art market).

<sup>319</sup> See *id.* at 14 (explaining that “the central characteristic of twenty-first-century contemporary art is that traditional artist skills of composition and coloration have become secondary to originality, innovation, and shock—however achieved. There are now few restrictions on methods or materials.”); MacMasters, *supra* note 11 (observing that “contemporary artists experiment a lot with techniques” in their work).

<sup>320</sup> MacMasters, *supra* note 11; see also *supra* subsection I.C.2 (discussing how various Decrees have expanded the type of work accepted under *Pago en Especie*).

<sup>321</sup> Finance Act 2012, c. 14, sch. 14, pt. 4, para. 22(1)(a) (Eng.).

some discretion, it is doubtful that more contemporary forms of art and cultural property will be accepted because they have not yet had time to establish their cultural significance.

A second challenge unique to *Pago en Especie* is determining *who* can participate. Should only artists with well-established careers be able to pay taxes with their artwork, or should every artist have this opportunity? How should the SHCP decide which artists are “famous” enough? Perhaps to avoid making these difficult decisions, *Pago en Especie* currently allows *all* visual artists to participate, regardless of whether they are famous or obscure. One rationale behind this policy is that “[e]merging artists who aren’t important today might be important tomorrow.”<sup>322</sup> Nonetheless, since artists of all skill levels can submit artwork, some of the art collected is questionable in terms of quality and remains in storage.<sup>323</sup> One artist has said, “There are many very bad artists who pay in kind. It’s deceitful.”<sup>324</sup> Such a perception, even if untrue, could be damaging for *Pago en Especie*: how can the program justify writing off taxes for art of poor quality? Frankly, it cannot. Cognizant of this weakness, in 2014 an administrator hinted that changes to improve the quality of the works accepted might be forthcoming.<sup>325</sup>

If the United States were to adopt a payment-in-kind income tax for art, the IRS would first have to decide *what kind of art* would qualify.<sup>326</sup> Would it only accept permanent visual art? Or, would it accept art that is less conventional and even ephemeral, such as temporary installations or performance art? From a policy perspective, it might be immensely difficult to justify these decisions when people value various styles and schools of art differently. Second, the IRS would have to determine *which artists* are worth collecting.<sup>327</sup> Is the work of a locally acclaimed ceramist to be treated the same as that of an internationally acclaimed painter who has had fifteen gallery shows in New York City?<sup>328</sup> Ultimately, if perceived as arbitrary and inequitable, these determinations could foment resentment among taxpayers and imperil a system that tries to make decisions precisely and impartially.

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<sup>322</sup> Johnson, *supra* note 14.

<sup>323</sup> *Id.* (“If the program has a fault, it may be that the state takes too much art.”).

<sup>324</sup> *Id.* (quoting sculptor, wood craftsman, and lithographer Victor Guadalajara).

<sup>325</sup> *Id.*

<sup>326</sup> When considering whether estates should be allowed to pay estate taxes with art, Merryman and Elsen argue that “[a]ny legislation to authorize payment of taxes with art must accordingly provide a basis for distinguishing the art that will be acceptable and the art that will not be (the alternative of accepting all art is clearly out of the question).” MERRYMAN & ELSEN, *supra* note 237, at 1040. This same argument applies to paying income taxes with art as well.

<sup>327</sup> See Melián, *supra* note 104 (explaining that this would be a challenging determination to make).

<sup>328</sup> *Id.*

Currently, the IRS depends on qualified experts and the Art Advisory Panel to assess the value of artwork donated for tax deductions;<sup>329</sup> however, these specialists make *no determinations* about whether the art is or is not worth collecting.<sup>330</sup> For example, if the Philadelphia Museum of Art wanted to accept the donation of an obscure painting or a sculpture of decaying organic matter, the Art Appraisal Service would not interfere and question whether the painting or the sculpture is “worthy” of a tax deduction. Instead, it would defer to the Philadelphia Museum of Art’s decision to accept the work and verify its fair market value if the donor valued it at \$50,000 or more. In this way, the IRS leaves questions about whether a particular piece is artistically “worthy” to the art community and the public at large. From a policy perspective, the IRS should continue to distance itself from such subjective decisions. They would be difficult—if not impossible—to justify, and would damage the perception that the IRS collects taxes impartially, objectively, and precisely. Instead, the United States should avoid a payment-in-kind income tax scheme and allow museum directors, curators, collectors, artists, and the general public to determine *what* and *who* is worth collecting.

#### E. *Payment-in-Kind Programs May Set a Dangerous Precedent*

Once a government establishes a payment-in-kind tax program for art, other taxpayers may demand similar treatment. Currently, Mexico allows only visual artists to pay income taxes in kind.<sup>331</sup> However, will Mexico’s contemporary writers soon demand access to a program like *Pago en Especie*? Will musicians request to pay with compositions to benefit the cultural identity of the nation? Will landowners with valuable mineral deposits eventually want to pay their income taxes in kind? For the United Kingdom, CGS is less likely to raise these questions because many different objects can be considered preeminent, including manuscripts, books, art, scientific items, or any other object that the relevant Minister deems worthy.<sup>332</sup> Nonetheless, *Pago en Especie* has explicitly favored visual artists and it may prove difficult to defend that position if other taxpayers demand a similar payment-in-kind scheme.

The United States would certainly face similar challenges if it adopted a payment-in-kind scheme for art or cultural property. Somewhat surprisingly,

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329 INTERNAL REVENUE SERV., PUB. NO. 561, DETERMINING THE VALUE OF DONATED PROPERTY (2007), <https://www.irs.gov/pub/irs-pdf/p561.pdf> [<https://perma.cc/2Q7M-LRC9>].

330 See *supra* subsections III.B.4–5.

331 See Decree of 2006, *supra* note 84, art. 12 (permitting visual artists who employ less traditional materials to participate in *Pago en Especie*); Decree of 1994, *supra* note 12, art. 1 (limiting participants to visual artists who sell paintings, graphics, and sculptures); MacMasters, *supra* note 11 (describing how *Pago en Especie* has recently broadened the type of art accepted).

332 Finance Act 2012, c. 14, sch. 14, pt. 4, para. 22 (Eng.).

the United States has allowed at least three estates to pay *estate taxes* in kind with various objects, but these involved unique circumstances and required special legislative authorization.<sup>333</sup> In each instance, the federal government perceived certain objects to be valuable enough to accept in place of cash; thus, the estates were allowed to give rare coins, forestland, and photographic plates to the government and receive a tax credit against their respective estate taxes.<sup>334</sup> These cases, however, were clearly the exception, not the norm. If the IRS were to begin accepting art and cultural property as payment for income taxes, it may have trouble refusing tax payments in short stories, songs, minerals, land, or oil. Thus, from a policy standpoint, it would be better to retain a system of cash payments and only allow indirect tax deductions for art owners.

F. *Payment-in-Kind Programs Could Undermine the Principles of Fairness, Objectivity, and Precision in the United States' Tax System*

The federal income tax system depends greatly on taxpayers to report information about their earnings and to ascertain their tax obligations.<sup>335</sup> Although the IRS oversees this process, its purpose is “to help the large majority of compliant taxpayers with the tax law, while ensuring that the minority who are unwilling to comply pay their fair share.”<sup>336</sup> Thus, taxpayers are responsible for initiating their tax filings. To ensure that taxpayers continue to report their earnings accurately and their tax obligations honestly, upholding the moral force of the federal tax system is imperative. Policies and decisions that appear inequitable, arbitrary, or imprecise may be particularly damaging<sup>337</sup> and cause taxpayers to lose faith in the system’s ability to “enforce the law with integrity and fairness to all.”<sup>338</sup>

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333 See Rhodes, *supra* note 181, at 292-99 (recounting how the federal government allowed three different estates to satisfy their estate taxes with material property); see also Glassman, *supra* note 181 (explaining how New Mexico permitted the Georgia O’Keeffe estate to satisfy some of its estate taxes with art).

334 See Rhodes, *supra* note 181, at 292-99 (describing the property accepted by the government in lieu of cash payments).

335 See INTERNAL REVENUE SERV., THE TRUTH ABOUT FRIVOLOUS TAX ARGUMENTS 1-2 (Jan. 2015), <https://www.irs.gov/PUP/taxpros/The%20Truth%20Jan%202015.pdf> [<https://perma.cc/34NA-39VA>] (describing our system of “voluntary compliance” as one that “allow[s] taxpayers initially to determine the correct amount of tax and complete the appropriate returns, rather than have the government determine tax for them from the outset”).

336 *The Agency, Its Mission and Statutory Authority*, I.R.S., <http://www.irs.gov/uac/The-Agency,-its-Mission-and-Statutory-Authority> [<https://perma.cc/GYQ3-6AUB>] (last updated Oct. 26, 2015).

337 See, e.g., Kelsey Snell, *Two Years After Scandal, the IRS Still Struggling*, WASH. POST (Aug. 5, 2015), <http://www.washingtonpost.com/news/powerpost/wp/2015/08/05/two-years-after-scandal-the-irs-still-struggling> [<https://perma.cc/3RPU-RAZ9>] (exemplifying the gravity of an allegation that the IRS scrutinized the tax returns of certain political nonprofits more closely than others).

338 *The Agency, Its Mission and Statutory Authority*, *supra* note 336.

Emulating payment-in-kind tax programs such as *Pago en Especie* and CGS may jeopardize the principles of fairness, objectivity, and precision that sustain the current tax system. Allowing visual artists to pay taxes with art could prompt taxpayers to question why artists are treated preferably to engineers, architects, and musicians—all of whom could claim a certain artistry in their professional work. Similarly, offering payment-in-kind opportunities for those who are wealthy enough to collect art and cultural property could prompt taxpayers to question why the less wealthy or less artistically inclined have no choice but to pay in cash. Additionally, the process of selecting and valuing art and cultural property introduces subjective opinions into a system that prides itself on objective and precise calculations.<sup>339</sup> Ultimately, a payment-in-kind program might enrich our sense of cultural identity and our national collections, but it would impoverish the integrity of our tax system. Instead, the United States must preserve and protect its system of collecting taxes in cash to uphold the principles of fairness, objectivity, and precision inherent in a tax scheme based on the compliance of taxpayers.

#### CONCLUSION

Relative to *Pago en Especie*, CGS is a preferable payment-in-kind model for several reasons. First, because CGS has a fixed annual cap on the amount of tax credit it can award, it avoids forfeiting more revenue than it can afford to lose. In contrast, *Pago en Especie* has never estimated how much tax it has forgone or what the collection is worth, essentially insulating the program from any sort of meaningful economic assessment. Second, because CGS collects items with a well-established history and value, it can justify forgoing cash revenue to a certain extent. *Pago en Especie*, however, must accept artwork without regard for its value or prominence. Third, CGS is less likely to set a precedent for other payment-in-kind tax programs because many types of preeminent objects qualify for a tax reduction; conversely, *Pago en Especie* may prompt Mexico's writers or musicians to demand similar opportunities to pay their taxes in kind. Finally, CGS appears more equitable because it allows anyone who owns a preeminent object to offer it in exchange for a tax reduction, while *Pago en Especie* only exempts visual artists from cash payments.

Despite these relative advantages and safeguards however, the United States should not emulate CGS, *Pago en Especie*, or any other payment-in-kind system. Collecting art to enrich the nation's cultural heritage is certainly more alluring than scrutinizing tax tables, calculating deductions, and writing checks,

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<sup>339</sup> See INTERNAL REVENUE SERV., 1040 INSTRUCTIONS: 2015 (2016), <http://www.irs.gov/pub/irs-pdf/i1040gi.pdf> [<https://perma.cc/LD6H-YMKP>] (providing tables and worksheets to help taxpayers determine the exact tax owed).



but policymakers must consider all of the implications of such a scheme. Ultimately, the United States should reject a payment-in-kind income tax program because it would (1) forfeit valuable cash revenue in a direct and partial manner; (2) commit public funds to the care and conservation of the accepted art; (3) disadvantage private museums; (4) force the IRS to make subjective decisions about what kind of art is worth collecting; (5) create a dangerous precedent for others to demand payment-in-kind schemes; and (6) introduce preferential treatment and subjectivity into a system founded on fairness, objectivity, and precision. Although taxpayers may grumble about the tedium of tax paperwork or the headaches involved in calculating the amount of a charitable tax deduction, by requiring cash payments the United States treats taxpayers impartially, upholds clear, objective standards, and makes precise valuations. A payment-in-kind income tax, though perhaps artful and alluring in appearance, would ultimately prove harmful to the integrity and success of our federal income tax system.

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