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AN OBJECTIVE APPROACH TO THE VALUATION OF WORKS OF ART DESTROYED WHILE ON CONSIGNMENT IN ILLINOIS GALLERIES

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INTRODUCTION

In February and April of 1989, a sprinkler system caused a small flood, and two fires occurred in a warehouse full of art galleries on Superior and Huron Streets in the River North area of Chicago. A renovation of the building was in progress. A small portion of one gallery's collection was sent to a conservator following the February flood and was not in the building at the time of the fires. The second fire raged overnight on April 15-16, 1989, destroying the building and most of its contents, but approximately 4,000 artworks were recovered from the ashes and thereafter sent to a storage facility where they remain today.

A lawsuit consolidating over twenty cases is now pending in the Circuit Court of Cook County,² and two lawsuits have been filed in the United States District Court for the Northern District of Illinois.³ In the Cook County case, galleries are suing the construction companies involved in the renovations; artists are suing the galleries and construction companies; one man who was injured during the fire is suing the construction companies; and insurers are suing to recover payments made to various aggrieved parties or to determine which company should be responsible for paying which claims. In the federal court cases, artists are suing galleries.

Scores of artists have not yet filed suit.⁴ Although a number of artists settled with gallery owners outside the litigation, the claims in the Cook County case alone exceed \$34 million.

The cause of the April 15-16, 1989 fire remains unknown, despite years of discovery, expert analyses and a Chicago Fire Department report suggesting that arson was not involved. Thus, it will be up to a Cook County jury to decide who was to blame for the fire.

Even more vexing than the liability issue, however, is the quantification of the amount of damages that the "liable" party or parties will be called upon to pay. Galleries are claiming damages not only for their lost furnishings, equipment and business opportunities, but also for the loss of their inventories—the art. Some of the artworks were purchased outright by the

galleries or their owners, but most of the art was on consignment, *i.e.*, in possession of the galleries for the purpose of being sold. The artists, therefore, have competing claims to damages for their lost artworks. Only the insurers' subrogation claims are undisputed, since the sums they paid are certain.

The main problem in the River North cases, thus, is how to evaluate the damaged or destroyed artworks in order to compensate the galleries and artists for their losses. Are the artworks that were damaged during the flood or were recovered from the ashes salvageable? Unlike the valuation of fungible goods in comparison with readily available sources, establishing the value of a destroyed artwork which may have been unique is problematical and often subjective.

Artworks are not priced for sale merely on the cost basis of the materials used by the artist to create them. Rather, the artist and gallery agree on a rather subjective evaluation of what the market can bear, or what a reasonable buyer of artworks might pay for a piece. That list price is determined at the time of consignment, but may change over the years that an artwork remains in the gallery's collection or as an artist becomes recognized so that his or her artworks are in demand. Some artists enjoy regular and repeated sales, while others may not see their works sold until the gallery mounts an exhibit spotlighting their art.

The fair market value of a damaged or destroyed artwork is very difficult to ascertain. Determining the aggregate amount of damages in the River North cases, thus, presents an awesome challenge. Lengthy testimony by the artists, the gallery owners and even experts could be necessary to verify value. However, unlike situations involving existing works of art, the artworks in the River North case are either gone or in such damaged condition that art appraisers might not be able to provide adequate assistance to the courts on evaluating the losses.

Adding to that dilemma is the fact that galleries and artists usually share in the proceeds from a sale of a consigned artwork. The gallery retains a percentage of the gross sale price as a sales commission,

sometimes subtracting additional charges called “discounts” if the artworks are sold through other dealers or to collectors requiring discounts. The gallery is then supposed to pay the artist the balance.

Thus, the galleries involved in the River North case could assert claims to a commission-percentage of the values established for the lost artworks. Artists, on the other hand, could be entitled to full compensation for their losses since they did not receive any benefit from the gallery’s consignment.

Few legal authorities exist on the very complex concept of art valuation, especially in the context of destruction while on consignment. No writers have yet proposed a mathematical model on which art valuations could be made. Accordingly, this article attempts to establish both a legal basis and an objective framework for evaluating works of art that have been damaged or destroyed while consigned to Illinois galleries.

LEGAL AUTHORITIES ON ART VALUATION

Only one reported opinion specifically addresses art valuation in the context of destruction during a gallery fire.⁵ That case construes the California Consignment of Art Act.⁶ The Illinois Consignment of Art Act⁷ has not yet been construed in reported opinions by the courts.⁸

Internal Revenue Service regulations and Tax Court decisions provide some guidance regarding valuation of art in the context of charitable contribution deductions and estate tax returns. General measure-of-damages cases in Illinois provide additional approaches to the valuation of damaged or destroyed personal property, but do not address the unique properties and valuation characteristics of artworks.

Nonetheless, the existing authorities offer a legal basis not only for measuring the damages applicable to the artworks lost in the River North fire, but also for what types of evidence are sufficient to quantify such damages. The evidence then can be transformed through mathematical formulae into actual damages quantifications. *See*, Formulae For Establishing Valuation Of Damaged or Destroyed Artworks, below.

Pelletier v. Eisenberg

The *Pelletier* opinion is the only existing ruling on valuation of artworks destroyed during a gallery fire.⁹ In that case, the jury awarded the artist \$21,689 (for the fair market value at the time of destruction of nine paintings destroyed in the gallery fire), \$2,816 (for future income losses attributable to the lost potential for sales of the nine paintings), \$42,500 (for time and monies spent by the artist in pursuit of insurance proceeds withheld by the gallery owner), and pre-judgment interest on the insurance proceeds.¹⁰

On appeal of cross-motions for judgment notwithstanding the verdict or for a new trial, the California

appellate court affirmed the trial court’s decision to conduct a new trial on damages incurred by the artist because of the alleged conversion of the insurance proceeds by the gallery owner.¹¹ The court, however, affirmed the jury’s verdict as to both types of damages awarded to the artist for the lost paintings—fair market value and future losses.

With regard to the loss-of-artwork damages, the defendant gallery owner argued on appeal that the “fair market value” and “future losses” amounts awarded by the jury to the artist should be reduced by the commissions the gallery was due. The court disagreed, citing specific provisions of the California Consignment of Art Act.¹²

The *Pelletier* court found that the California Act defines a consignee as a trustee of the artworks for the benefit of the artist.¹³ The Act also precludes consignees from reducing their exposure to fiduciary liability to consignors through contracts.¹⁴ Accordingly, the court found the gallery owner to be strictly liable for damages to or destruction of consigned artworks.¹⁵

Additionally, the *Pelletier* court found that the typical consignment agreement between the artist and gallery contemplated the sharing of revenues only from sales of artworks, not from the destruction of them. Here the artist was denied his benefit of the consignment bargain. He suffered not only the loss of potential sales, but also an accompanying deleterious effect on the expected increase in his reputation from future sales. The gallery owner should pay what the jury awarded—both the total fair market value of the artworks at the time of destruction and a rationally derived figure for future sales losses, without subtracting the gallery owner’s commission percentage.¹⁶

The Illinois Consignment of Art Act

Illinois’ Consignment of Art Act includes provisions substantially identical to California’s statute.¹⁷ Additionally, the Illinois Act expressly provides that the consignee/gallery will be strictly liable to the artist for damages to or destruction of consigned artworks.¹⁸ Clearly, the purpose of a consignment of art agreement is the same in Illinois as it is in California.

The only difference between the California and Illinois statutes is the Illinois limitation on the artist’s reimbursement if a consigned artwork is damaged or destroyed.¹⁹ In Section 2(5), the Illinois Act provides that the artist’s recovery in such a situation is limited to what s/he would have received if the artwork had been sold.²⁰

That limitation applies, however, *only* when a valid consignment contract exists between the artist and the consignee, as described in Section 1405 of the Illinois Act.²¹ That Section requires a written consignment contract which must include at least five provisions: (1) the value of the artwork consigned; (2) the time within which proceeds of sales are to be paid by the consignee to the artist; (3) the commis-

sion percentage the consignee will be due upon the sale of the artwork consigned; (4) the minimum price for which the artwork can be sold; *and* (5) a description of discounts, if any, that will be applied by the consignee to such sales.

If a consignee fails to comply with the contract provisions of the Illinois Act, of course, the consignee cannot invoke the limitation-of-damages provision. Section 1405(3), in fact, permits the artist to seek the assistance of the courts in having the artist's "obligations" voided. An artist's only obligation under the Act is to pay the gallery commissions. Therefore, it is clear that an artist, whose works are destroyed while in constructive trust to a consignee/gallery that has *not* complied with the Act, is entitled to full recovery.²² The voiding of the artist's obligations, thus, renders the gallery strictly liable for both the fair market value of and future losses reasonably expected from the artist's works.

Illinois Legal Authorities on Valuation of Fungible Goods

As did the *Pelletier* court, Illinois authorities establish the initial measure of damages for destroyed personal property as the fair market value of the property. For example, the Seventh Circuit has held:

[T]he owner of destroyed goods is entitled to be put in as good a position pecuniarily as if his property had not been destroyed and that the proper criterion to be used in measuring damages is the value of the thing destroyed. Whether the goods are totally destroyed or are only damaged, the fair market value is nonetheless the proper measure...²³

Illinois courts follow the fair-market-value rule for damages to fungible goods, adding that the fair market value should be measured at the time just immediately prior to destruction.²⁴ In such cases, the following indicia of value have been permitted as evidence of the fair market value of the damaged goods: salvage income, plus the cost of salvaging; catalog prices, plus lost profits; reasonable prices that a consumer would pay; insurance coverage appraisals; and tax depreciation schedules

In the River North cases involving destroyed artworks, however, salvage and appraisals are not possible.²⁵ Some artists were prominent enough to have had catalogs with prices of their artworks, but tax schedules are not available for specific artworks lost in a fire. More importantly, artworks are unique, non-fungible goods and thus, cannot be evaluated from publicly available pricing data for "similar" goods.

Illinois Legal Authorities on Valuation of Unique Goods

Illinois authorities support the award of something more than mere fair market value when the destroyed property is unique or of special personal value to the owner.²⁶

In *Jensen v. Chicago & Western Indiana Railroad Co.*, a case involving antique railroad cars, the court found that the property to be valued was not "an ordinary object of commerce" and was so unique that it "may not be susceptible to the general measure of damages." In such instances, the property's value must be ascertained "from such elements as are attainable."²⁷ The proper basis for determining compensatory damages to a "unique" piece of personal property is its actual value to the plaintiff/owner.²⁸

In *Jankoski v. Preiser Animal Hosp., Inc.*, the court was faced with evaluating damages due to a dog owner. Following a rationale similar to the *Jensen* court's, the *Jankoski* court found that "the plaintiff is entitled to demonstrate [the dog's] value to him by such proof as the circumstances admit."²⁹

At a minimum, the language from these two opinions suggests that an artist's own valuations of unique personal property should be considered and given weight in measuring damages. Thus, to quantify the fair market value of the artworks at the time of the River North fire, the list prices stated by each artist are reasonable and proper values at which to begin an evaluation inquiry. It stands to reason that an artist will sell no works if they are over-priced. Artists, therefore, will seek only what the market can bear, given the artists' own impressions of the value of their artworks—a subjective evaluation on the basis of medium, style, prior market experience, reputation, etc.

In *Gannon v. Freeman*, the court held that "the law does not require the plaintiff to prove the exact amount of his loss; it is sufficient that the evidence provide a basis for assessing damages with a fair degree of probability."³⁰ The court found that the original cost of a vintage automobile, the cost of the parts plaintiff purchased to restore it, and the time plaintiff spent on its restoration were sufficient indicia of value for the destroyed car.

Unfortunately, those indicia do not apply to artworks. Especially when an artwork was never sold prior to its being consigned, no cost basis will exist. Also, the value of an artwork does not necessarily reflect the cost of its materials and the time it took the artist to create it. As mentioned above, the value of an artwork is subjective, based on a combination of the artist's, gallery owner's and art buyer's impressions of what it is worth.

Internal Revenue Service Regulations And Tax Opinions

Treasury Regulations define fair market value 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 the relevant facts.”³¹ The same rule is found in the estate tax regulations.³² The estate tax regulations provide additionally that the fair market value of an item of personal property is to be determined in the market where such items are “most commonly sold to the public.”³³

These definitions imply that personal property must be evaluated in the context of its own specific, ultimately efficient marketplace. The marketplace is where the appropriate consumers would purchase the property at retail prices.³⁴ The most appropriate comparable market for valuation purposes is the most active retail marketplace for the particular item involved.³⁵ The appropriate retail price is the best and lowest that the consumer actually would have had to pay.³⁶

In *Biagiotti v. Commissioner*, the Tax Court was concerned with Pre-Columbian artworks imported from South America. The tax payer purchased the artworks over a period of years, held them for the statutorily required periods and then donated them to a museum. The Internal Revenue Service claimed that the tax payer’s valuations of the donated artworks were inflated.

In resolving the “battle of the experts” which is typical of tax court disputes over art valuation, the Tax Court found evidence of auction sales incompetent.³⁷ Comparable sales in the retail markets for Pre-Columbian artworks, however, were both competent and reliable.³⁸

In *Anselmo v. Commissioner*, the court was concerned with a tax shelter in which poor quality, semi-precious gems were imported from South America and later donated to a museum at the prices they would have received if set in costume jewelry. The court relied on the complete definition of fair market value established in the estate tax regulations, including the example provided therein for automobiles (the fair market value of an automobile is what a car of similar age, make, model, condition and description would earn from a sale to the general public, not what it would earn if sold to a used car dealer). The court found the price at which a consumer could purchase the stones at the time of donation to be their fair market value.³⁹

In the case of artworks consigned to a gallery, the market for the artists’ works is the art-buying public who frequent the galleries to which the artworks were consigned looking for artworks offered at retail prices. Therefore, evidence of an artist’s comparable sales in other retail markets would be reliable for the

purpose of evaluating destroyed artworks.

Evidence of comparable sales has been used primarily in the area of real property valuations. The standards for valuing real property, however, are very different from those for valuing personal property, especially artworks.⁴⁰

The rule “is one of relevancy and not unlike the general evidentiary rule applied in all proceedings requiring similarity of conditions.”⁴¹ The property selected for comparison must be “similar in kind and character.”⁴²

One of the few cases that deals with the comparisons of works of art involved a painting by Jean Baptiste Camille Corot, a 19th century French painter.⁴³ In *Furstenberg v. United States*, the tax payer had donated a figure painting by Corot to a university. In arguing against the Internal Revenue Service’s imposition of a tax deficiency, the tax payer produced evidence of the price at which another Corot figure painting had just recently been sold to a collector. The recent sales price was substantially higher than the price the tax payer paid for her Corot figure painting.⁴⁴

Initially, the Court found the scope of “comparables” to have been properly limited by the experts. Ninety-five percent of Corot’s paintings had been landscapes.⁴⁵ His landscapes were extremely popular in the 19th century, while his figure paintings were almost unknown in that period. In the 20th century, that situation reversed itself.⁴⁶ Impliedly, a comparison of sales of Corot landscapes with sales of Corot figure paintings would not have been permitted.

The *Furstenberg* court, however, did not accept the tax payer’s argument that the recently sold Corot figure painting was comparable. Relying on the experts’ testimony, the court found that the painting at issue had been damaged by a negligent restoration prior to its donation to the university and that it was of inferior artistic quality compared to the high-priced Corot.⁴⁷ Given the tax payer’s cost basis; the very high price of the recently sold painting; the general quality and condition of the tax payer’s Corot; the potential for its being restored properly; and the general upward price trend in the retail art marketplace, the court found the tax payer’s Corot to be worth half what she had reported, but substantially more than what the Internal Revenue Service’s panel of appraisers estimated as its fair market value, which had been less than her cost basis.

ANALYSIS

According to the above-cited authorities, the artists whose artworks were destroyed while consigned to the River North galleries are entitled to the fair market value of their artworks at the time of the fire, plus an additional amount to compensate them for future losses.⁴⁸ The problem, then, is how to calculate those values.

Fair market value at the time of the April, 1989 fire could be established through documentary evidence, including consignment sheets or agreements with the gallery owners on retail prices for each artwork at the time it was consigned; up-dated price lists or catalogs reflecting prices of the destroyed works contemporaneous with the fire; or proof of prices from sales of other comparable works around the time of the fire. The artists' subjective valuations of what prices would have applied to each artwork at the time of the fire, however, are also reliable.

Future losses also could be established through documentary evidence, including proof of prices from recent sales of comparable works; recent consignment sheets or agreements with gallery owners for comparable works; recent price lists or catalogs reflecting comparable works; or general inflation rates in the retail art sales. An artist's estimate of what the same artwork would sell for today is an excellent starting place for evaluating future losses. A mere subtraction of the earlier value from the later value, however, would not provide a reasonable valuation of future losses. An evaluation of future losses, therefore, could be based on a particular artist's sales history with a gallery, on the 13% figure established in *Pelletier*, or on any data revealing how many comparable artworks an artist sells each year.

To the extent an artist can provide sufficient information, detailed computations based on mathematical formulae will provide estimates of both fair-market-value and future-losses amounts to a reasonable degree of reliability. See, *Formulae for Establishing Valuation of Damaged or Destroyed Artworks*, below.

Only if sufficient information is not available would more evidence be needed. For example, an artist's testimony could provide guidance especially with regard to pricing practices depending on the size, medium and date of an artwork. Additionally, art appraisers or experts could offer opinions as to comparability, whether slides or catalog reproductions are available for both the destroyed and recently sold works, and on general inflation rates in retail art sales.

The simplest means of resolving the River North artists' claims involving destroyed artworks would be to accept the artists' estimates of fair market value and future losses. The most time-consuming means would be to require testimony of the artists and other experts. The middle ground between the two extremes might be to accept the artists' estimates after having them calculate as best they can using the formulae suggested below.

FORMULAE FOR ESTABLISHING VALUATION OF DAMAGED OR DESTROYED ARTWORKS

I. Fair market value

The following are valuation categories, ascertainable from various kinds of evidence, which could be used to establish the fair market value of destroyed artworks at the time of the April, 1989 fire:

A. Cost Basis ("CB"): The cost of materials, plus a reasonable hourly rate for the artist's time spent on creating the artwork; the most recent price at which the artwork actually sold prior to the consignment; or the price of a comparable work sold prior to consignment revealing the minimum fair market value of a similar artwork prior to the time of consignment.

B. Prices quoted at time of consignment, or Consignment Value ("CV"): Prices could appear in consignment sheets, or have been quoted orally and accepted by the gallery owner.

C. Price Lists or Guidelines at time of the fire, or Price List Value ("PLV"): Some artists regularly update their price lists, but most have size/sales history guidelines that they use to establish pricing of their artworks, along with reasonable increases.

D. Comparable Prices or Sales at time of the fire, or Comparable Price ("CP"): Evidence of comparable prices or sales may be as specific as prices for identical prints (in the case of multiples), but usually will be based, of necessity, on substantial similarity of works in the same style, size and medium.

E. Comparable Prices or Sales after the fire, or Recent Value ("RV"): Price lists or sales records for substantially similar works.

F. Expert Opinions: As a last resort, if none of the above-described information is available, art valuation experts and art appraisers can provide estimates of fair market value and probabilities of sales, as well as comparisons among comparable artists' works within the same type of market place.

Cost Basis (CB), as indicated in the tax cases analyzed above, does not provide a reasonable basis for evaluating the fair market value of an artwork unless no other information is available. If only the Cost Basis is known, an expert may be required to provide a basis for extrapolating the minimum value of an artwork to its fair market value at the time of the fire. The Cost Basis, however, does suggest a minimum value against which the other ascertainable figures can be compared for reliability.

From the other categories of information described above, the following calculations are possible (in order of reliability) to establish fair market value at the time of the fire:

If there is reliable documentary evidence only for

Price List Value (PLV) or Comparable Price (CP), no additional evidence or calculations should be necessary. The Price List Value (PLV) or Comparable Price (CP) is the fair market value, according to the legal authorities cited above.

If there is reliable documentary evidence only for Consignment Value (CV) and Recent Value (RV), revealing a disparity between the two values, those figures can be used to extrapolate fair market value at the time of destruction. Statistical packages and sophisticated calculators can perform an annual-percent-of-increase (A_p) analysis through a "nth root" calculation, by taking the root to the power of the number of years' difference (N) between two values (CV and RV) of the figure reached from dividing the later value (RV) by the earlier value (CV) to reach A_p . To reach FMV at the time of destruction, add the original CV to CV plus the A_p to reach the following year's increased value (IV) for each year after consignment until the year of the fire.

Formulae:

$$\sqrt[n]{\frac{RV}{CV}} = A_p$$

$$CV + (V \cdot A_p) = IV_1$$

$$IV_1 + (IV_1 \cdot A_p) = IV_2$$

$$IV_2 + (IV_2 \cdot A_p) = IV_3, \text{ etc. until } IV_n \text{ is } 1989$$

II. Future Losses

Future losses could be calculated simply by applying the 13% figure established in *Pelletier*. On the other hand, future losses could be specifically related to a particular artist's dealings with a particular gallery and calculated in a more complex manner. The value of the complex calculation lies in its ability to evaluate the history of an artist's sales from a particular gallery in relation to the value of the particular collection consigned to that gallery, taking into consideration that artist's percentage of estimated annual increases in value.

The complex calculation would require a number of separate calculations to determine future losses: (1) determining the artist's percentage of annual increase (A_p) calculated from any two years for which collection values are available; (2) finding an average of the artist's annual sales prior to the fire (S89), either from the particular gallery or from comparable markets; (3) using those figures to estimate total anticipated sales for all years since the fire until the gallery's collection would have been depleted (TS); and (4) subtracting the fair market value of the whole collection in 1989 (FMV89) from the total anticipated

sales (TS) to reach a figure for future losses (FL). If an artist does not have data revealing a sales history with the gallery, the same calculations can be performed, but with a different means of approximating average 1989 sales (S89). See, *Future Losses Without Sales From The Gallery*, below.

A. Percentage of Annual Increase (A_p)

Finding the artist's percentage of annual increase (A_p) requires the same "nth root" calculation described above: calculating the root to the power of 3 (representing the number of calendar years that have passed since the April 15, 1989 fire) of what the gallery's collection would have been worth currently (V_{92}), divided by fair market value of the collection in 1989 (FMV₈₉) to equal the A_p .

Formula:

$$\sqrt[n]{\frac{V_{92}}{FMV_{89}}} = A_p$$

B. Estimated Average Annual Sales

Finding an artist's estimated average sales for the year of the fire (S89) requires a series of calculations, each taking available sales figures for years prior to the fire (S85, S86, S87, S88) and applying the percentage of annual increase (A_p) for all years through 1988, to extrapolate a figure for estimated sales in 1989 (S89). To establish what the artist's average sales would have been in 1989, average all of each prior year's sales figures (S89_{yr1}, S89_{yr2}, S89_{yr3} through 1988, S89₈₈) and divide by the number of years for which sales figures exist (N).

Formulae:

(assuming the availability of four years' worth of sales figures from 1985 through 1988 and 1989 being the year of the fire):

$$S85 \cdot A_p = S86_{85} \cdot A_p = S87_{85} \cdot A_p = S88_{85} \cdot A_p = S89_{85}$$

$$S86 \cdot A_p = S87_{86} \cdot A_p = S88_{86} \cdot A_p = S89_{86}$$

$$S87 \cdot A_p = S88_{87} \cdot A_p = S89_{87}$$

$$S88 \cdot A_p = S89_{88}$$

$$S89_{85} + S89_{86} + S89_{87} + S89_{88} \div 4 = S89$$

C. Total Anticipated Sales

Once the estimated 1989 average sales figure (S89) is established, a spread-sheet calculation program or step-by-step manual calculations can be utilized to subtract yearly sales from the collection of artworks (FMV_x) to reach each successive year's remaining inventory (I₈₉, I₉₀, I₉₁, etc.). By applying the percentage of annual increase (A_p) to each year's remaining inventory, a fair market value for that remaining inventory (FMV₈₉, FMV₉₀, FMV₉₁, etc.) can be reached. Then, by applying the percentage of

annual increase (A_p) to the previous year's sales, that year's estimated sales (S_{90}, S_{91}, S_{92} , etc.) can be reached and subtracted from each year's remaining inventory at fair market value (FMV_x) until the collection of artworks in the gallery is depleted (when the last remaining FMV_x amount is less than the previous year's sales). The sum of all yearly estimated sales (S_{89}, S_{90}, S_{91} , etc.) and the last FMV_x amount equals the total estimated sales (TS) for that artist, i.e., the amount that would put the artist in the same position s/he would have been in had the artworks not been destroyed in the fire.

Formulae:

$$FMV_{89} - S_{89} = I_{89} \cdot A_p = FMV_{90} - (S_{89} \cdot A_p = S_{90}) = I_{90}$$

$$\cdot A_p = FMV_{91} - (S_{90} \cdot A_p = S_{91}) \cdot A_p = I_{91} \cdot A_p = FMV_{92} - (S_{91} \cdot A_p = S_{92}) \cdot A_p = I_{92} \cdot A_p = FMV_{93}$$
, etc. until the final year's FMV_x is less than the prior year's estimated sales figure (S_x)

$$S_{89} + S_{90} + S_{91} + S_{92} + FMV_{y,x} = TS$$

D. Future Losses

The difference between the artist's total estimated sales (TS) and the collection's 1989 fair market value (FMV_{89}) is the artist's future losses (FL).

Formula:

$$TS - FMV_{89} = FL$$

E. Future Losses Without Sales From the Gallery

For some artists whose works were consigned just prior to the fire or for whom no specific gallery sales records are available, the future loss computations based on prior sales from a particular gallery cannot be performed. FL for such artists can be calculated, however, as long as there is some sales history for the artist. For example, the average 1989 sales figure (S_{89}) for such artists could be derived from averaging the number of works (N) in the collection at their FMV_{89} to reach an average price per work (AP) and multiplying that figure by the average number of sales (AS) per year that the artist has enjoyed over the years. S_{89} can then be used to compute future losses in the same manner discussed above.

Formula:

$$FMV_{89} \div N = AP \times AS = S_{89}$$

III. Damages

Each artist's damages (D) should be the sum of fair market value (FMV), plus future losses (FL).

Formula:

$$FMV_{89} + FL = D$$

IV. Sample Calculations

The following calculations show how the damages for two different artists (Artist A and Artist B) are established through the use of the formulae suggested above. The calculations presume that both artists' estimates of fair market value at the time of the fire and currently are reliable. Artist A had a prior history of sales with the gallery and a large collection in the gallery at the time of the fire, while Artist B had no sales history with the gallery and a small collection in the gallery at the time of the fire.

Artist A	Artist B
$\sqrt[3]{\frac{\$69,800(FMV_{89})}{\$49,400(FMV_{89})}} = 1.1221291(A_p)$	$\sqrt[3]{\frac{\$11,600(FMV_{89})}{\$8,200(FMV_{89})}} = 1.1225733(A_p)$
<i>Percentage of Annual Increase in Collection Values</i>	

Projected 1989 Sales

S87 = \$ 3,225	S87 = 0
S88 = \$11,500	S88 = 0
$\$3,225 \times 1.1221291 = \$3,618.87$	$(8,200/4) = 2,050 \times 1 = 2,050$
$\$3,618.87 \times 1.1221291 = \$4,060.84 (S_{89_{87}})$	(given Artist's record of selling one work per year in comparable markets)
$\$11,500 \times 1.1221291 = \$12,904.49 (S_{89_{88}})$	
$(\$4,060.84 + \$12,904.48)/2 = \$8,482.67 (S_{89})$	

Estimated Damages Due

$\$49,400 (FMV_{89}) - \$8,482.67 (S_{89}) = \$40,917.33 (I_{90})$	$\$8,200 (FMV_{89}) - \$2,050 (S_{89}) = \$6,150.00 (I_{90})$
$\cdot 1.1221291 = \$45,914.54 (FMV_{90})$	$\times 1.1225733 = \$6,903.83 (FMV_{90})$
$\$45,914.54 (FMV_{90}) - (\$8,482.66 \cdot 1.1221291 = \$9,518.64 (S_{90})) = \$36,395.90 (I_{91}) \cdot 1.1221291 = \$40,840.90 (FMV_{91})$	$\$6,903.83 (FMV_{90}) - (\$2,050.00 \cdot 1.1225733 = \$2,301.28 (S_{90})) = \$4,602.55 (I_{91}) \cdot 1.1225733 = \$5,166.70 (FMV_{91})$
$\$40,840.90 (FMV_{91}) - (\$9,518.64 \cdot 1.1221293 = \$10,681.14 (S_{91})) = \$33,843.12 (FMV_{92})$	$\$5,166.70 (FMV_{91}) - (\$2,301.28 \cdot 1.1225733 = \$2,583.36 (S_{91})) = \$2,583.34 (I_{92}) \cdot 1.1225733 = \$2,899.99 (FMV_{92})$
$\$33,843.12 (FMV_{92}) - (\$10,681.14 \cdot 1.1221291 = \$11,985.62 (S_{92})) = \$21,857.50 (I_{93}) \cdot 1.1221291 = \$24,526.94 (FMV_{93})$	$\$2,899.99 (FMV_{92}) - (\$2,583.34 \cdot 1.1225733 = \$2,899.98 (S_{92})) = \$.01 (I_{93}) \cdot 1.1225733 = \$.01 (FMV_{93})$

\$24,526.94 (FMV₉₃) -
 (\$11,985.62 • 1.1221291 =
 \$13,449.41 (S93)) =
 \$11,077.53 (I₉₄) • 1.1221291
 = \$12,430.42 (FMV₉₄)

\$8,482.66 (S89)	\$2,050.00 (S89)
9,518.64 (S90)	2,301.28 (S90)
10,681.14 (S91)	2,583.36 (S91)
11,985.62 (S92)	2,899.98 (S92)
13,449.41 (S93)	.01 (FMV ₉₃)
<u>12,430.42 (FMV₉₄)</u>	<u>\$9,834.63 (TS = D)</u>
\$66,547.89 (TS = D)	<u>-8,200.00 (FMV₈₉)</u>
<u>-49,400.00 (FMV₈₉)</u>	\$1,634.63 (FL)
\$17,147.89 (FL)	

CONCLUSION

The April, 1989 River North gallery fire has created both a challenge and an opportunity for the Illinois courts. The challenge lies in streamlining and standardizing the evidence required for establishing a fair measure of damages for the galleries and artists that lost artworks in the fire. The opportunity lies in establishing precedents that will enable others whose artworks are damaged or destroyed to evaluate similar, unfortunate losses. Hopefully, the analyses and formulae offered in this article will assist the courts in meeting both the challenge and opportunity, and the galleries and artists in obtaining adequate redress.

1. Patricia A. Felch established ARTSLAW Offices of PATRICIA A. FELCH in January, 1992, to concentrate in arts and entertainment law, representing creative companies and individuals in the protection of their creations through copyrights, trademarks, business formations, contracts and litigation. Ms. Felch obtained Bachelor and Master of Arts degrees in Music History and Literature and a Master of Librarianship degree from the University of Denver and served as an arts and music librarian for the Atlanta Public Library and Northwestern University. In 1987, she obtained a J.D. from Loyola University of Chicago School of Law and began representing artists and arts-related businesses in their legal needs. Ms. Felch has taught music and humanities courses in Illinois' community colleges and now teaches entertainment law courses at Columbia College in Chicago. She wishes to thank Jennifer Fischer, who as a law clerk assisted in the initial research for this article and is now an attorney, and Adam Ingber, who transformed Ms. Felch's calculation theories into the formulae and quantifications offered in this article.

2. *Dubina v. Mesirow Realty Dev., Inc.*, 89 CH 03332 (Cir. Ct. Cook County, Ill. 1989) (consolidated).

3. *Davis v. Rowe*, 91 C 2254 (Cir. Ct. Cook County, Ill. 1991); *Allegretti v. van Straaten*, 93 C 1287 (Cir. Ct. Cook County, Ill. 1993).

4. This author has represented more than a dozen artists whose artworks were consigned to the van Straaten Gallery. Two artists settled with the gallery without filing suit in early 1990, and three opted not to pursue their claims. Another ten artists have recently filed a joint action to be consolidated into the Cook County case, in order to preserve their rights against the construction companies which are subject to the four-year statute of limitations in section 13-214 of the Illinois Code of Civil Procedure (ILL. REV. STAT. ch. 110, para. 13-214 (1992), now 735 ILCS 5/13-214).

5. *Pelletier v. Eisenberg*, 177 Cal. App. 3d Supp. 558 (1986).

6. CALIF. CIV. CODE §§ 1738.1 *et seq.* (West Supp. 1993).

7. ILL. REV. STAT. ch. 121 1/2, para. 1400 *et seq.* (Smith-Hurd

Supp. 1992) (now 815 ILCS 320/0.01 *et seq.*).

8. The Honorable Albert Green, however, did find the Illinois Consignment of Art statute constitutional during proceedings in a case currently pending in the Circuit Court of Cook County. *Dubina*, 89 CH 03332.

9. *Pelletier v. Eisenberg*, 177 Cal. App. 3d 558 (1986).

10. David Semelsberger, now of Endeman, Lincoln, Turek & Heater in San Diego, California, was one of the trial and appellate defense attorneys in the *Pelletier* case. He reported during an April, 1992 telephone conversation with this writer the following details of the *Pelletier* proceedings. Mr. Pelletier, the artist, produced at trial not only consignment contracts and price lists to establish the fair market value of the works he lost in the gallery fire, but also a gallery owner who testified about the current worth of the artist's paintings then being exhibited based on recent sales. The artist also testified at length as to where comparable pieces had been sold (and for how much) and where comparable pieces were currently exhibited (and for what prices). As to future losses, the artist claimed that he was going to lose potential income not only from future sales of the individual paintings that had been destroyed (for which he produced evidence of increases in his own income as well as comparable sales), but also from the reprint market in posters, post-cards, calendars, etc. (for which he produced an expert who testified that about 13% of the fair market value of a painting could be earned in reproductions). Mr. Semelsberger noted that, except for one painting which all parties agreed was the artist's best, the "future losses" awarded by the jury were approximately 13% of the "fair market value" amounts, which was consistent with the expert's testimony on reproduction profits as well as the artist's evidence of the increases in value of his comparable artworks.

11. This issue has not yet been raised in the River North cases.

12. *Pelletier v. Eisenberg*, 177 Cal. App. 3d at 566.

13. CALIF. CIV. CODE § 1738.6 (c) (West Supp. 1993).

14. CALIF. CIV. CODE § 1738.8 (West Supp. 1993).

15. *Pelletier v. Eisenberg*, 177 Cal. App. 3d at 567.

16. *Id.* at 566-567.

17. *See*, ILL. REV. STAT. ch. 121 1/2, para. 1402(3) (consignee is trustee of artworks for the benefit of the artist) and para. 1406 (contractual waivers of liability are void) (now respectively 815 ILCS 320/2(3) and 815 ILCS 320/6).

18. ILL. REV. STAT. ch. 121 1/2, para. 1402(5) (now 815 ILCS 320/2(5)).

19. *Id.*

20. *Id.*

21. ILL. REV. STAT. ch. 121 1/2, para. 1405 (now 815 ILCS 320/5).

22. Although discovery in the River North cases pending in Cook County is not yet completed, it appears that two of the galleries did not comply with the Illinois Consignment of Art Act. The Peter Miller Gallery did not use consignment contracts at all, and the consignment sheets issued by the van Straaten Gallery included only the title of the artworks consigned, the stated list price of each piece and an inventory number. Some of the van Straaten sheets also included language limiting the gallery's exposure in the event of damage or destruction of the consigned artworks to the cost of materials, in derogation of the Illinois Consignment Act. Thus, arguably, the artists represented by those two galleries should be entitled to full recovery.

23. *H.K. Porter Co. v. Halperin*, 297 F.2d 442, 445 (7th Cir. 1961) (citing *Standard Oil Co. of N.J. v. Southern Pac. Co.*, 268 U.S. 146 (1925)).

24. *See*, *Madigan Bros. v. Melrose Shopping Ctr.*, 556 N.E.2d 730, 735 (Ill. App. Ct. 1990) (tools damaged on one floor of a building during a fire allegedly caused by co-tenants' use of a gas burner on the floor below); *Behrens v. W.S. Bills and Sons, Inc.*, 283 N.E.2d 1, 7 (Ill. App. Ct. 1972) (partial damage to fixtures and inventory of children's clothing store after wall to adjoining property collapsed); *Williams-Bowman Rubber Co. v. Industrial Maintenance, Welding & Mach. Co.*, 677 F. Supp. 539, 541 (N.D. Ill. 1987) (both personal and real property damages resulting from

fire); *Tozzi v. Testa*, 423 N.E.2d 948 (Ill. App. Ct. 1981) (home furnishing store goods and fixtures damaged during fire).

25. Additionally, artists who have learned that their artworks were being treated for water damage caused by the February, 1989 flood or were recovered from the ashes of the April 15-16, 1989 fire deny the salvageability of their artworks. Although modern technology can restore some kinds of paintings and sculptures, a mere smudge or wrinkle in a work on paper ruins its potential for sale. The artists, therefore, may disclaim the artworks that were not actually destroyed in the fire, pursuant to the Visual Artists' Rights Act of 1989 (17 U.S.C. §§ 101, 106A (Supp. 1991)).

26. *Gannon v. Freeman*, 431 N.E.2d 1303, 1305 (Ill. App. Ct. 1982) (vintage automobile damaged beyond repair during an automobile accident); *Jensen v. Chicago & W. Ind. R.R.*, 419 N.E.2d 578 (Ill. App. Ct. 1981) (antique, restored railroad cars sold for salvage when restorer failed to remove them from leased premises); *Jankoski v. Preiser Animal Hosp., Ltd.*, 510 N.E.2d 1084, 1086 (Ill. App. Ct. 1987), *cert. denied*, 517 N.E. 2d 1086 (Ill. 1987) (dog with no fair market value, but personal value to its owner).

27. *Jensen v. Chicago & W. Ind. R.R.*, 419 N.E.2d at 594.

28. *Id.*

29. *Jankoski v. Preiser Animal Hosp., Ltd.*, 510 N.E.2d at 1087.

30. *Gannon v. Freeman*, 431 N.E.2d at 1305.

31. Treas. Regs. § 1.170-1(c)(1) (as amended in 1972).

32. Treas. Reg. § 20.2031-1(b) (as amended in 1965).

33. *Id.*

34. *See, Anselmo v. Commissioner*, 757 F.2d 1208, 1214 (11th Cir. 1985); *Biagiotti v. Commissioner*, 52 T.C.M. (CCH) 588, 593 (1986).

35. *Biagiotti v. Commissioner*, 52 T.C.M. at 593.

36. *Anselmo v. Commissioner*, 757 F.2d at 1213.

37. The opinion does not reveal the court's reasoning for the distinction, other than a suggestion that auction markets are different from retail markets. The difference could be substantial or

nonexistent. For example, an auction house, like Leslie Hindman Auctioneers in Chicago, often establishes a beginning auction bid (on the basis either of the least amount the seller will accept or a thoroughly researched appraisal of a piece) and deals both with very sophisticated buyers and impulse shoppers. A gallery, on the other hand, may accept the artist's list price and have no latitude in negotiating a lower or higher price, while selling only within the gallery to browsers or through dealers buying for collectors or corporations. In other words, the same artwork could sell for the same amount in both markets, or the sales prices could vary substantially, depending on the sophistication of the buyer.

38. *But see contra, Lightman v. Commissioner*, 50 T.C.M. (CCH) 266 (1985) (auction prices and bulk sales prices were appropriate for measuring the value of paintings for which a market existed only in auctions or bulk sales).

39. *Anselmo v. Commissioner*, 757 F.2d at 1213-14.

40. *See, Williams-Bowman Rubber Co. v. Industrial Maintenance, Welding & Mach. Co., Inc.*, 677 F. Supp. at 540-541 (N.D. Ill. 1987) (juxtaposing Illinois' simple standards for evaluating personal property with the confusingly conflicting cases on real estate valuations).

41. *Department of Pub. Works and Bldgs. v. Seeber*, 235 N.E.2d 269, 272 (Ill. App. Ct. 1968).

42. *DuPage Bank and Trust Co. v. Property Tax Appeal Bd.*, 502 N.E.2d 1250, 1254 (Ill. App. Ct. 1986), *cert. denied*, 484 U.S. 1004 (1988).

43. *Furstenberg v. United States*, 595 F.2d 603 (Cl. Ct. 1979).

44. *Id.* at 608.

45. *Id.* at 606.

46. *Id.*

47. *Id.* at 609.

48. The Illinois Consignment of Art Act also provides for reimbursement of expenses, including attorneys' fees. ILL. REV. STAT. ch. 121 1/2, para. 1407 (now 815 ILCS 320/7).