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International Art and Cultural Heritage

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I. Laches and "Spoils of War" Doctrine: *In re Flamenbaum*

The New York Court of Appeals decision in *In re Flamenbaum* established the elements of the laches defense to a replevin claim for the recovery of stolen cultural objects and rejected any "spoils of war" doctrine that would allow a thief to acquire valid title to stolen property.[1] A German team of archaeologists conducted excavations in the early part of the twentieth century at the site of Ashur, located in what is today northern Iraq. Among finds discovered was a small gold tablet dating to the reign of the Assyrian king Tukulti-Ninurta I (1243 to 1207 BC). The tablet, approximately the size of a modern credit card, contained an inscription in Assyro-Babylonian written in the Middle Assyrian cuneiform script.[2] The tablet arrived in the Berlin Museum (now the Vorderasiatisches or Near Eastern Museum) in 1926. The museum was closed during World War II and the objects, including the gold tablet, were put in storage. At the end of the war, however, the tablet was missing.

The tablet was next discovered in the estate of Riven Flamenbaum ("the decedent"), a Holocaust survivor who, at the time of his death in 2003, was a resident of Long Island,

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1. *In re* Flamenbaum, 899 N.Y.S.2d 546 (2010), *rev'd*, 945 N.Y.S.2d 183 (App. Div. 2d Dep't. 2012), *aff'd*, 22 N.Y.3d 962 (2013). The following description of the facts is taken from the Court of Appeals decision, 22 N.Y. 3d 962, at 963-65.

2. The tablet was published in the excavation report. WALTER ANDRAE, DIE JÜNGEREN ISCHTAR-TEMPEL IN ASSUR 53, pl. 24, p-q (1935). Contrary to the court's description, the tablet was found near the inner city wall to the north of the Ishtar temple. The tablet documents the completion by Tukulti-Ninurta I of the temple of Ishtar of Nineveh at Assur, which was begun by his father Shalmaneser I. The temple itself has not been located, so this tablet and two others found with it are the only records of its existence. Email from Prof. John Russell to author (Nov. 25, 2013) (on file with author).

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New York. At the time of the estate's accounting, a son of the decedent notified the museum of the tablet's location. The museum then filed a claim in Surrogate's Court in Nassau County to recover the tablet. The estate defended against the museum's claim, arguing that the museum was barred under New York State's doctrine of laches and that the decedent might have acquired good title to the tablet as a "spoil of war."[3]

While New York courts follow the "demand and refusal" rule, which holds that a cause of action for the recovery of stolen property accrues (thus triggering the running of the statute of limitations time period) only after the original owner demands return of the stolen property from a good faith possessor and the possessor refuses,[4] a claim may be barred through the equitable defense of laches.[5] Because claims involving recovery of stolen art and other cultural objects are generally litigated in federal court based on diversity jurisdiction, the New York courts have spoken infrequently on the elements of a laches defense and their application to specific cases. This case, however, presented an opportunity for the New York Court of Appeals to articulate how the defense of laches should apply.

The Surrogate's Court held that the museum's claim should be barred by laches, based on the museum's failure to report the tablet's disappearance to authorities or to record its theft on international registries of stolen art. The Surrogate's Court found that this lack of activity on the museum's part prejudiced the estate's ability to defend against the museum's claim.[6] The Appellate Division reversed the Surrogate's Court, holding that the estate, which had the burden to prove the elements of its affirmative defense, failed to establish that the museum had acted unreasonably or that the estate suffered legal prejudice.[7] On further appeal, the New York Court of Appeals affirmed the Appellate Division's decision.

The significant aspect of the Court of Appeal's decision focused on the two prongs of the laches defense—that the claimant delayed unreasonably and that the defendant established that the unreasonable delay caused prejudice to the defendant. In this case, the court held that the estate failed to prove that the museum's failure to publicize the loss of the tablet and any delay on the part of the museum resulted in the museum's failure to discover that the decedent possessed the tablet before his death.[8] The estate also failed to establish that it suffered any prejudice due to the museum's alleged delay.[9]

In discussing the question of prejudice, the court focused on whether there was any legal theory by which Flamenbaum might have acquired good title to the tablet, an admittedly stolen object. The estate relied on a theory of "spoils of war" according to which a Russian soldier or the Russian government might have acquired title to the tablet through conquest and as a "spoil of war." In addition to the fact that the estate offered no proof

3. *In re* Flamenbaum, 22 N.Y.3d 962, 964-65 (2013).

4. *See* Kunstsammlungen zu Weimar v. Elicofon, 678 F.2d 1150 (2d Cir. 1982); Menzel v. List, 267 N.Y.S.2d 804 (Sup. Ct. 1966), *modified by* 279 N.Y.S.2d 608 (App. Div. 1967), *rev'd*, 298 N.Y.S.2d 979 (1969).

5. *See* Bakalar v. Vavra, 819 F. Supp. 2d 293 (S.D.N.Y. 2011), *aff'd*, 500 Fed. App'x 6 (2d Cir. 2012); Solomon R. Guggenheim Found. v. Lubell, 569 N.E.2d 426 (N.Y. 1991); *In re* Peters, 821 N.Y.S.2d 61 (App. Div. 1st Dep't 2006); Wertheimer v. Cirker's Hayes Storage Warehouse, 752 N.Y.S.2d 295 (App. Div. 2002).

6. *In re Flamenbaum*, 899 N.Y.S.2d at 553–54.

7. *Id.*

8. *In re Flamenbaum*, 22 N.Y.3d 962, 965–66 (2013).

9. *Id.* at 966.

for such a theory, the Court of Appeals squarely rejected the notion that the decedent could have acquired title in this way, stating that "we decline to adopt any doctrine that would establish good title based upon the looting and removal of cultural objects during wartime by a conquering military force . . . . Allowing the [e]state to retain the tablet based on a spoils of war doctrine would be fundamentally unjust."[10]

This decision is significant for two reasons. First, it clearly establishes that the laches defense is not based merely on a claimant's alleged unreasonable delay. Even if the claimant has delayed, the defendant must prove that the delay caused legal prejudice and prevented the defendant from proving a defense.[11] Second, the court provided a clear rejection of a "spoils of war" doctrine that would permit acquisition of title to stolen property. The United States has rejected the idea that legitimate war booty includes artworks and cultural objects since 1863 when the Lieber Code was adopted for the U.S. Army during the Civil War.[12] The international community has also rejected such a notion since the 1899 and 1907 Hague Conventions, to which all nations involved in World War II were and still are States Parties.[13] It is also worth noting that the Court of Appeals, however, did not limit its rejection of a "spoils of war" doctrine to World War II, and so it may remain to future claims to determine whether such rejection applies to cultural objects taken during earlier wars and conflicts.

II. The Fair Use Defense: *Cariou v. Prince*

Litigation between the artists Patrick Cariou and Richard Prince has raised, again, questions of the definition of the fair use defense in a copyright infringement case and, in particular, the meaning of the transformative use element of the defense. In 2000, photographer Patrick Cariou published a book titled *Yes, Rasta*, which contained photographs taken in Jamaica by Cariou over a six-year period.[14] The book contained photographs of Rastafarians, other individuals, and landscapes in Jamaica.[15] After its publication, artist Richard Prince obtained a copy of *Yes, Rasta*.

From approximately December 2007 through February 2008, Prince exhibited artwork in St. Barths, including a collage titled *Canal Zone*, which contained thirty-five photographs torn from a copy of *Yes, Rasta*.[16] *Canal Zone* was not sold, but Prince did sell other

10. *Id.*

11. Prejudice can be either evidence-based or expectations-based. As the First Circuit in Vineberg v. Bissonnette stated, "[t]ypically, the kind of prejudice that will support a laches defense arises out of a loss of evidence, the unavailability of important witnesses, the conveyance of the property in dispute for fair market value to a bona fide purchaser, or the expenditure of resources in reliance upon the status quo ante." Vineberg v. Bissonnette, 548 F.3d 50, 57 (1st Cir. 2008).

12. FRANCIS LIEBER, INSTRUCTIONS FOR THE GOVERNMENT OF ARMIES OF THE UNITED STATES IN THE FIELD ¶ 36 (1898) ("[i]n no case shall they [works of art, libraries, collections] be sold or given away, if captured by the armies of the United States, nor shall they ever be privately appropriated, or wantonly destroyed or injured").

13. Hague Convention Respecting the Laws and Customs of War on Land, art. 56 (Oct. 18, 1907) 36 Stat. 2277, T.S. No. 539, *available at* http://avalon.law.yale.edu/20th_century/hague04.asp ("[a]ll seizure of, destruction or wilful [sic] damage done to institutions of this character, historic monuments, works of art and science, is forbidden, and should be made the subject of legal proceedings").

14. Cariou v. Prince, 784 F. Supp. 2d 337, 343 (S.D.N.Y. 2011).

15. *Id.*

16. *Id.*

works of art from that exhibit through the Gagosian Gallery, Inc. (the Gagosian Gallery).[17] Prince eventually created twenty-nine collages and paintings in a series titled *Canal Zone* and twenty-eight of those works contained images from *Yes, Rasta* (the Works).[18] In November and December 2008, Prince exhibited twenty-two of the Works in the Gagosian Gallery, which also published a catalog that included images of many of the Works.[19]

Cariou sold a limited number of photographs to people he knew, but otherwise he had not sold or licensed any of the photographs from *Yes, Rasta*.[20] Cariou did negotiate with a gallery owner named Christiane Celle to exhibit photographs from *Yes, Rasta* in her New York gallery (the Celle Gallery).[21] When Celle became aware of Prince's show at the Gagosian Gallery, she cancelled the show at the Celle Gallery.[22] Cariou filed a petition alleging copyright infringement against Prince, the Gagosian Galley, Larry Gagosian, and Rizzoli International Publications, Inc. Prince, the Gagosian Gallery, and Gagosian (collectively the Defendants) asserted the defense of fair use.

On March 18, 2011, the federal district court granted Cariou's motion for summary judgment.[23] The district court held that (1) the transformative use element weighed heavily against a finding of fair use; (2) Prince's use and exploitation of the photographs were substantially commercial; (3) Defendants acted in bad faith; (4) the nature of the work factor weighed against a finding of fair use; (5) the factor of amount and substantiality of the portion used weighed heavily against a finding of fair use; (6) the factor of effect of use upon the potential market for or value of the copyrighted work weighed against a finding of fair use; and (7) the Gagosian Gallery and Gagosian were liable as direct, vicarious, and contributory infringers.[24]

The district court permanently enjoined the Defendants from any further copyright infringement.[25] It gave the Defendants ten days to deliver to Cariou the works and associated materials to be destroyed or disposed of as Cariou saw fit.[26] Finally, the district court ordered the Defendants to notify all current and future purchasers of the works that they infringe on Cariou's copyrights, were not made legally, and cannot be lawfully displayed.[27] The Defendants appealed.

On April 25, 2013, the Court of Appeals for the Second Circuit reversed in part, vacated in part, and remanded the action to the district court.[28] The Defendants contended that Prince's work was transformative and constituted fair use.[29] The Defendants argued that the district court erred by requiring that, in order to rely on the defense of fair use, the works must comment on Cariou, his work, or an aspect of popular culture associated

17. *Id.*
18. *Id.* at 344.
19. *Cariou*, 784 F. Supp. 2d at 344.
20. *Id.*
21. *Id.*
22. *Id.*
23. *Id.* at 355.
24. *Id.* at 337.
25. *Cariou*, 784 F. Supp. 2d at 355.
26. *Id.* at 355–56.
27. *Id.* at 356.
28. Cariou v. Prince, 714 F.3d 694 (2d Cir. 2013).
29. *Id.* at 698.

with Cariou or his work.[30] The Court of Appeals ruled that the fair use defense included no such comment requirement and that twenty-five of the works were protected as a matter of law by fair use.[31]

The Court of Appeals concluded that those twenty-five works "have a different character, give Cariou's photographs a new expression, and employ new aesthetics with creative and communicative results distinct from Cariou's."[32] The Court of Appeals clarified that this conclusion should not be taken to suggest that any cosmetic changes to Cariou's photographs would necessarily constitute fair use, as a subsequent work may modify the original without being transformative.[33] The Court of Appeals determined that, in those twenty-five works, Prince did not present the same material as Cariou in a different manner; instead, he added something new to them "and presented images with a fundamentally different aesthetic."[34] As those twenty-five works were found not to infringe Cariou's copyrights, the Court of Appeals found that Gagosian and Gagosian Gallery could not be held liable as vicarious or contributory infringers.[35]

The Court of Appeals remanded to the district court the issue of the five remaining works for the district court to determine whether any of them infringed on Cariou's copyrights and whether they were entitled to the defense of fair use.[36] The Court of Appeals expressed no view as to whether those five works are entitled to the defense of fair use.[37] Cariou filed a petition for a writ of certiorari with the U.S. Supreme Court. On November 12, 2013, that petition was denied.[38]

III. The Act of State Doctrine and the Foreign Sovereign Immunities Act: *De Csepel v. Republic of Hungary* and *Konowaloff v. Metropolitan Museum of Art*

Two cases reviewed by appellate courts in late 2012 and early 2013 shared the act of State doctrine and its application as a common defense. In *Konowaloff v. Metropolitan Museum of Art*, the Second Circuit affirmed the district court and permitted the defendant to rely on the act of State doctrine.[39] But, in *de Csepel v. Republic of Hungary*, the D.C. Circuit affirmed a district court decision that rejected defenses based on the act of State doctrine and the Foreign Sovereign Immunities Act (FSIA).[40]

The act of State doctrine prohibits U.S. courts from examining

> the validity of a taking of property within its own territory by a foreign sovereign government, extant and recognized by this country at the time of suit, in the absence

30. *Id.*
31. *Id.* at 698–99.
32. *Id.* at 707-08.
33. *Cariou*, 714 F.3d at 707–08.
34. *Id.*
35. *Id.* at 712.
36. *Id.*
37. *Id.* The district court mistakenly referred to twenty-nine works when, in fact, there were thirty.
38. Cariou v. Prince, 714 F.3d 694 (2d Cir. 2013) *cert. denied*, 134 S. Ct. 618 (2013).
39. Konowaloff v. Metro. Museum of Art, 702 F.3d 140, 148 (2d Cir. 2012), *aff'g* No. 10-CV-09126, 2011 WL 4430856, at *1 (S.D.N.Y. Sept. 22, 2011).
40. De Csepel v. Republic of Hungary, 714 F.3d 591, 603–04 (D.C. Cir. 2013).

> of a treaty or other unambiguous agreement regarding controlling legal principles, even if the complaint alleges that the taking violates customary international law.[41]

This also applies if the taking violates the foreign State's own law. Act of State issues arise only "when the outcome of the case turns upon the effect of official action by a foreign sovereign."[42]

In *Konowaloff*, the plaintiff was "the sole heir to the estate of his great-grandfather, Ivan Morozov," who had a modern art collection that allegedly "ranked 'among the finest in Europe'" prior to World War I.[43] In 1911, Morozov acquired the subject painting by Paul Cezanne, *Madame Cezanne in the Conservatory* (the Painting).[44] Following the Russian Revolution in March 1917, power was seized by the Bolshevik regime and its successor the Union of Soviet Socialist Republics (collectively referred to as the Soviet Government), which were not recognized by the United States until November 1933.[45] In December 1918, the Bolsheviks decreed Morozov's collection, including the Painting, to be the property of the State, which plaintiff alleged was an act of theft.[46] The amended complaint further alleged that the Painting was acquired illegally in 1933 by Stephen Clark (who eventually donated it to the Metropolitan Museum of Art in 1960) when he purchased it from Knoedler, one of the galleries representing the Soviet Government in the sale of art.[47] In sum, the plaintiff alleged that both the acquisition of the Painting by the Bolsheviks in 1918 and the subsequent sale to Stephen Clark violated Russian law and were both characterized as an "act of party, not an act of [S]tate."[48]

The Second Circuit held that the act of State doctrine was a bar to plaintiff's case and upheld the dismissal by the district court.[49] In doing so, the court reasoned that, "[f]irst, the characterization of the Soviet government's appropriation as 'an act of theft' is a legal assertion, which the court was not required to accept" and "[s]econd, the lawfulness of the Soviet government's taking of the Painting is precisely what the act of state doctrine bars the [U.S.] courts from determining."[50] Additionally, the court rejected any consideration of the 1933 sale stating that the relevant act of State was the 1918 appropriation by the Soviet Government, upon which "Morozov was deprived of all his property rights and interests in the Painting."[51] Finally, the court held that even though "the current Russian government is apparently disinclined to engage in further appropriations of private property and has initiated an investigation into the 1930s art sales . . . it has not repudiated the 1918 appropriation that is the government act that deprived Morozov, and hence Konowaloff, of any right to the Painting."[52]

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41. Banco Nacional de Cuba v. Sabbatino, 376 U.S. 398, 428 (1964); *see also* Republic of Austria v. Altmann, 541 U.S. 677, 713 (2004).
42. W.S. Kirkpatrick & Co. v. Envtl. Tectonics Corp., 493 U.S. 400, 406 (1990).
43. *Konowaloff*, 702 F.3d at 141.
44. *Id.*
45. *Id.* at 141–42.
46. *Id.* at 142.
47. *Id.* at 143–44.
48. *Konowaloff*, 702 F.3d at 143–44.
49. *Id.* at 148.
50. *Id.* at 147 (citing Sosa v. Alvarez-Machain, 542 U.S. 692, 727 (2004)).
51. *Id.*
52. *Id.* at 148.

De Csepel involves the Herzog Collection, assembled by Baron Mor Lipot Herzog and said to have been the largest pre-World War II art collection in Hungary, comprising more than two thousand paintings, sculptures, and other artworks.[53] The Nazis allegedly seized large portions of the collection for eventual transport to Germany.[54] In the subject litigation, heirs of the Herzog family sought the return of at least forty works of art from the original collection that plaintiffs allege had been handed over by the Hungarian government to the Museum of Fine Arts for "safekeeping" and were eventually displayed in several institutions in Budapest, all named defendants.[55]

Plaintiffs asserted a primary claim for breach of bailment agreements as well as claims for "conversion, constructive trust, accounting, declaratory relief, and restitution based on unjust enrichment."[56] Defendants moved to dismiss on the grounds that the district court lacked jurisdiction under the FSIA, the complaint failed to state a claim for bailment, and the claims were barred by the act of State doctrine as well as by the applicable statute of limitations, the political question doctrine, and the doctrines of foreign *non conveniens* and international comity.[57] In most respects, the district court denied the defendants' motion to dismiss, including, among other reasons, the act of State doctrine.[58]

The court expended little time on the act of State doctrine and its application to these facts, correctly holding that the doctrine did not apply. Critical to its determination was the fact that plaintiffs were seeking "to recover from breaches of bailment agreements," which were "not sovereign acts, but rather *commercial* acts entitled to no deference under the act of [S]tate doctrine."[59] The court reiterated the rule that the doctrine "applies only to conduct that is by nature distinctly sovereign, i.e., conduct that cannot be undertaken by a private individual or entity."[60]

The D.C. Court of Appeals also affirmed the district court's decision finding that the FSIA did not apply to defendants. The FSIA prohibits U.S. courts from exercising jurisdiction over foreign States.[61] The Herzog heirs argued that the FSIA abrogated sovereign immunity based on the "expropriation" exception and, in the alternative, the "commercial activity" exception within the statute.[62]

The district court abrogated Hungary's sovereign immunity under the FSIA by relying on the expropriation exception, which states that a U.S. court has jurisdiction over a foreign nation where "rights in property taken in violation of international law are at issue."[63] But the appellate court declined to rule on the application of the expropriation exception. Rather, it emphasized plaintiffs' claims that bailment contracts were created and repudiated after the Hungarian government expropriated the paintings in concert with the Nazis during World War II.[64] Therefore, the court held that it need only apply the FSIA's

53. De Csepel v. Republic of Hungary, 714 F.3d 591, 594 (D.C. Cir. 2013).
54. *Id.* at 595.
55. *Id.*
56. *Id.* at 596.
57. *Id.*
58. *Id.* at 596–97.
59. *Id.* at 604 (quoting De Csepel v. Republic of Hungary, 808 F. Supp. 2d 113, 143 (D.D.C. 2011)).
60. *Id.* (quoting McKesson Corp. v. Islamic Republic of Iran, 672 F.3d 1066, 1073 (D.C. Cir. 2012)).
61. 28 U.S.C. § 1604 (2012).
62. *De Csepel*, 714 F.3d at 597.
63. 28 U.S.C. § 1605(a)(3) (2012).
64. *De Csepel*, 714 F.3d at 597–600.

commercial activity exception, which abrogates sovereign immunity where an action is based on an act that (1) "took place outside the territory of the United States," (2) was connected with a commercial activity, and (3) had a direct effect on the United States.[65] Discussing the second factor, the court held that defendants' actions were commercial because they were similar to the type of action in which a private party might engage in commerce.[66] Pertaining to the third factor, the court decided that there was an effect on the United States because Hungary promised to return artwork to Herzog heirs it knew resided in the United States.[67]

The appellate court rejected defendants' FSIA arguments based on legal, not factual, grounds. It remains to be seen whether the heirs of the Herzog family can establish particular facts supporting the creation and breach of a bailment contract; meanwhile, the fate of these artworks remains uncertain.

IV. Due Diligence in Art Market Transactions: *Davis v. Carroll*

Earl Davis (Davis) received, as gifts from his parents, many Stuart Davis artworks, including eight works that were the subject of this lawsuit (the disputed works).[68] Davis consigned the disputed works, along with many others, to Salander O'Reilly Gallery (the gallery), owned by Larry Salander (Salander). Davis and Salander had an oral agreement that included an understanding that the gallery would contact Davis for an updated pricing before selling any artwork or indicating an asking price. Davis did not file any U.C.C. financing statements to publicize his consignment interest in works delivered to the gallery.

In late 2005, two Stuart Davis works sold for record amounts at Christie's and Sotheby's. Thereafter, Davis and Salander had a disagreement, and Davis told Salander "to suspend all sales pending [Salander's] return of the works to [Davis] before [they] had any further discussion between him and [Davis]."[69] Salander agreed to suspend sales, return Davis's artworks, and pay Davis for the artwork already sold. Starting in January 2006 and continuing through the next two years, Davis regularly pressured Salander to return all of the works that Davis had placed on consignment. Salander kept promising to do so but always found an excuse to delay.

Davis was unaware that the gallery was caught in a web of unethical and illegal dealings that ultimately resulted in Salander's criminal conviction. Before the gallery collapsed, Salander engaged in a series of major transactions with Joseph P. Carroll (Carroll), a private art dealer. Over four months in 2006, Salander purported to sell, through a series of exchanges (2006 Exchanges), forty-four artworks to Carroll—including fifteen Stuart Davis works, eight of which are the disputed works in this case.

In 2009, Davis filed suit in the U.S. District Court for the Southern District of New York to recover the disputed works from Carroll, arguing that Carroll should have been alerted to signs of foul play and that Carroll's due diligence reflected commercial indiffer-

65. *Id.* at 598 (quoting Rong v. Liaoning Province Gov't, 452 F.3d 883, 888–89 (D.C. Cir. 2006)).
66. *Id.* at 599 (citing Republic of Argentina v. Weltover, Inc., 504 U.S. 607, 614 (1992)).
67. *Id.* at 601.
68. Davis v. Carroll, 937 F. Supp. 2d 390, 394–95 (S.D.N.Y. 2013).
69. *Id.* at 398.

ence to Davis' legal rights. Carroll asserted he had every reason to trust the gallery and that his due diligence was more than adequate. Davis then moved for summary judgment.

This case involved the application of the "entrustment doctrine," codified in Article 2 of the Uniform Commercial Code.[70] Entrustment applies when an owner of property transfers possession to a merchant who deals in goods of that kind, and the merchant then transfers the property to a buyer in the ordinary course of business. In such cases, the merchant can transfer all rights that the entruster had in the property. In this case, Carroll argued that he had acquired title under the entrustment doctrine by purchasing from Salandar, an art dealer. This case addresses the question of what is the standard of good faith that a purchaser, particularly an art merchant, must display in order to claim status as a buyer in the ordinary course of business.

The court stated that New York law requires a heightened duty of due diligence where a purchaser is presented with reason to suspect foul play in a sale.[71] This objective inquiry focuses on whether a sale was transacted in the shadow of red flags that should have put the purchaser on notice of potential illegality. Davis identified a number of such warning signs, such as evidence of the Gallery's financial difficulties, mixed signals regarding the Gallery's right to convey valid title to the disputed works, and "bargain basement" pricing.[72]

The court found that, even read in the light most favorable to Carroll, the record dictated a finding of important red flags. The single most important red flag under New York law consists of indications that the seller neither owns the work nor enjoys authority to sell it. In this case, the court found that "it is beyond doubt that Carroll should have been alerted by numerous signs to serious questions about" the gallery's authority to sell the disputed works.[73] In support of this conclusion, the court cited Carroll's indifference to provenance statements for many of the works that simply listed "Estate of the Owner" or citations in the cataloguing for the works to publications that listed Davis as the owner.[74]

The court noted that "it is a basic duty of any purchaser of an object d'art to examine the provenance for that piece, and Carroll repeatedly affirms that he fulfilled that duty."[75] The record showed that none of the documentation associated with the transfer of the works listed the Gallery as the owner, and Salander never told Carroll that he or the gallery did, in fact, own the works. Carroll could point to no document that listed the gallery as the owner. "To the contrary, the documents all listed 'Estate of the Artist' as the provenance, in contrast to the documentation for several other works involved in the same set of exchanges that identified Salander, [the gallery], or Salander's wife as the owner."[76] The court concluded that "even crediting Carroll and reading the facts in a light that flatters him, any reasonable juror would conclude that the 2006 Exchanges raised a significant red flag that should have placed Carroll on notice of the need for further inquiry."[77]

70. N.Y. U.C.C. §§ 403(2)–(3).
71. *Davis*, 937 F. Supp. 2d at 427.
72. *Id.*
73. *Id.* at 428.
74. *Id.*
75. *Id.* at 429.
76. *Id.*
77. *Davis*, 937 F. Supp. 2d at 431.

"New York law also identifies bargain basement prices as a critically important red flag in art transactions. That red flag was clearly present during the 2006 Exchanges, as separately evidenced by the fact that (1) Carroll valued these works at markedly higher prices shortly after acquiring them and (2) there was a significant discrepancy between the prices that Carroll paid in May 2006 and an expert's fair market value appraisal."[78]

"The 2006 Exchanges began when Salander called Carroll and mentioned an end of year 90 percent off sale. Carroll claim[ed] that he interpreted this comment as a joke, but the subsequent course of dealings between him and Salander casts it in a very different light."[79] The court found that "the total value exchanged in the 2006 Exchanges, accounting for fair market appraisals and the substantial discounts common to [the art market], should have alerted any savvy market participant to foul play."[80] "This conclusion [was] independently supported by a comparison of Carroll's payment for the fifteen Davis works ($1,445,000) and [an independent] appraisal of the fair market value of those works at the time of the 2006 Exchanges ($4,595,000)." The court stated, "[i]n other words, Carroll received a 68.55 percent discount from fair market value . . . . The prices afforded to Carroll would have put any reasonable market participant on notice of foul play."[81]

The court decided that a reasonable juror would conclude that Carroll's acquisition of the disputed works was not "free and clear of cause to suspect improper dealings."[82] The court noted that "bargain basement prices offered by Salander, along with a battery of irregular and suspicious issues . . . pertaining to [the Gallery's] ownership of and right to sell the eight Disputed Works, constituted red flags that triggered a duty of heightened inquiry on Carroll's part . . . ."[83] As a result, Carroll was actually or constructively on notice of the need for 'further verification' before" acquiring the disputed works, and he therefore did not qualify as a buyer in the ordinary course of business.[84] The court therefore granted Davis's motion for summary judgment. Carroll filed a Notice of Appeal in the Court of Appeals for the Second Circuit, but, shortly thereafter, the parties filed a stipulation withdrawing the appeal pursuant to Federal Rule of Appellate Procedure 42.[85]

V. Detroit Institute of Arts

After years of financial turmoil, on July 18, 2013, the City of Detroit (the City) filed a petition for relief[86] under Chapter 9 of Title 11 of the U.S. Code (as amended, the "bankruptcy code").[87] In addition to the more typical municipal bankruptcy concerns (the ability of the City to continue to provide essential services or to meet payroll or pension obligations), the City's filing has occasioned discussion of the fate of the Detroit Institute

78. *Davis*, 937 F. Supp. 2d at 432 (citing Brown v. Mitchell-Innes & Nash, Inc., 2009 U.S. Dist. LEXIS 35081, at *20–21 (S.D.N.Y. Apr. 24, 2009)); *see also* Interested Lloyd's Underwriters, 2005 U.S. Dist. LEXIS 25471, at *14 (S.D.N.Y. Oct. 21, 2005).
79. *Davis*, 937 F. Supp. 2d at 432.
80. *Id.*
81. *Id.* at 434.
82. *Davis*, 937 F. Supp. 2d at 434.
83. *Id.*
84. *Id.* at 437 (citing Porter v. Wertz, 416 N.Y.S.2d 254, 258 (N.Y. App. Div. 1979)).
85. Order, Davis v. Carroll, No. 13-2201-cv (2d Cir. Jul. 15, 2013), ECF No. 33.
86. Bankr. Pet. at 1, *In re City of Detroit*, No. 13-53846 (Bankr. E.D. Mich., filed July 18, 2013), ECF No. 1.
87. *See* 11 U.S.C. § 101 (2012).

of Arts (the DIA). "As Detroit files for bankruptcy," the *New York Times* reported, the day after the city's filing, that "the impressive collection of the Detroit Institute of Arts has become a political bargaining chip in a fight that could drag on for years between the city and its army of creditors, who have said in no uncertain terms that the artworks must be considered a salable asset."[88]

The question of the collections' fate arises because of the DIA's unusual structure, in which title to the collections is held by the City, not by a not-for-profit corporation or trust. This structure, though, was not always the case. The DIA's predecessor, the Detroit Museum of Art, was founded as a private, not-for-profit corporation in 1885. As early as 1893, the museum began receiving supplemental funding from the City.[89] In 1915, however, the Michigan Supreme Court held that, even though the museum had conveyed its buildings to the City and given the City minority representation on the museum's board, such appropriations violated the state constitution's restrictions on the lending of credit by the City to an entity other than a public or municipal agency.[90]

In response, in 1919, the Michigan legislature amended the Corporations for the Cultivation of Art statute[91] to provide that not-for-profit cultural or educational corporations could convey their property to the state or municipalities. The Detroit Museum of Art conveyed its collections to the City. Subsequently, the legislature authorized the city to once again appropriate monies to support the museum, newly christened the "Detroit Institute of Arts" (DIA).[92]

In the intervening ninety-four years, the DIA has emerged as one of the country's finest encyclopedic art museums. Its holdings include *The Wedding Dance* (ca. 1566) by Pieter Bruegel the Elder, *Self Portrait* (1887) by Vincent Van Gogh, *The Dreams of Man* (1550) by Tintoretto, *The Visitation* (1640) by Rembrandt, *Cotopaxi* (1862) by Frederic Church, *The Window* (1916) by Henri Matisse, *Orange Brown* (1963) by Mark Rothko, *Saint Jerome in His Study* (ca. 1440) by Jan van Eyck, *Selene and Endymion* (ca. 1628) by Nicolas Poussin, *Double Self Portrait* (1967) by Andy Warhol, and the Diego Rivera murals.

In the City's bankruptcy case, the critical questions for the future of the DIA and its collections are (1) "[c]an all or part of the DIA's collections be leveraged or monetized and the proceeds be used to pay the city's debt unrelated to the DIA and its operations" and (2) "[c]an the city's creditors compel the sale of some or all of the DIA's collections?" The brief answer to the first question is a qualified "yes." The brief answer to the second question is a qualified "no."

Under the bankruptcy code, a debtor's ownership of or interest in property is determined under state law. As a result, the DIA's structure, its relation to the City, the manner in which the collections were acquired, and any restrictions attached to particular works are all essential facts. In an opinion issued June 13, 2013, Michigan's attorney general concluded that the DIA's collections could not be "sold, conveyed, or transferred

88. Randy Kennedy & Monica Davey, *Detroit's Creditors Eye Its Art Collection*, N.Y. TIMES (July 20, 2013), http://www.nytimes.com/2013/07/20/arts/design/detroits-creditors-eye-its-art-collection.html.

89. *Detroit Institute of Art's Ballot Initiative*, D BUSINESS (July 9, 2012), http://www.dbusiness.com/DBusiness/July-August-2012/Detroit-Institute-of-Arts-Ballot-Initiative.

90. Detroit Museum of Art v. Engel, 153 N.W. 700, 703 (Mich. 1915).

91. *See* 1885 Mich. Pub. Acts 2, as amended by 1913 Mich. Pub. Acts 446.

92. Mark Stryker, *DIA in Peril: A Look at the Museum's Long, Tangled Relationship with Detroit Politics and Finances*, DETROIT FREE PRESS (Sept. 8, 2013), http://www.freep.com/article/20130908/ENT05/130905007.

to satisfy City debts or obligations."[93] In the Attorney General's view, when the City acquired the collections of the Detroit Museum of Arts (which held the collections in a public trust), the City accepted the trust obligation. That trust's purpose was then assumed by the City through the DIA and continues to attach to all subsequent acquisitions. However, the attorney general's opinion is not dispositive and has not been accepted by the City's Emergency Manager and other parties in interest. The City's Emergency Manager engaged Christie's to review and appraise certain portions of the DIA collections that the City believes are unrestricted and available to be monetized.[94]

The answer to the second question—whether the City's creditors can compel the sale of the DIA's collections—turns on the more limited role and authority that a municipal debtor's creditors have in a Chapter 9[95] case than creditors of a corporate or individual debtor would have in more common Chapter 7[96] (liquidation) or Chapter 11[97] (reorganization) cases. In Chapter 9 cases, creditors have fewer options available to them than they do in cases where a debtor is not a municipality. In Chapter 9, for instance, creditors cannot propose a competing plan (only the municipal debtor may propose a plan), they cannot convert the debtor's case to a case under Chapter 7, they cannot have a trustee appointed, and they cannot force the sale of municipal assets under state law. Where the City's creditors do have bargaining power is in their right and ability to vote on confirmation of any plan of adjustment that the city will propose.

A Chapter 9 debtor restructures its debts by proposing and confirming a plan of adjustment. Importantly, that plan allows the debtor to non-consensually modify its contractual obligations.[98] This enables the debtor to assume those contracts that are beneficial and to reject those that are burdensome. So, while a creditor cannot force the City to sell any DIA artworks, it can vote against any plan the city proposes that modifies the creditor's pre-bankruptcy contractual rights. The City's creditors cannot dictate the process, but they are parties at the table.

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93. Conveyance or Transfer of Detroit Institute of Arts Collection, Mich. Att'y Gen. Op. No. 7272 (June 13, 2013).

94. Corey Williams, *Christie's Check of Detroit's Art Done in October*, ASSOCIATED PRESS (Oct. 4, 2013), *available at* http://news.yahoo.com/christies-check-detroits-art-done-132922465.html; *see also* Sherri Welch, *Not All Gifts to DIA Were Donated with Strings Attached*, CRAIN'S DETROIT BUSINESS (May 30, 2013), http://www.crainsdetroit.com/print/article/20130529/BLOG009/130529862/not-all-gifts-to-dia-were-donated-with-strings-attached.html.

95. *See* 11 U.S.C. §§ 901–46 (2012) (Adjustment of Debts of a Municipality). Chapter 9 of the Bankruptcy Code provides for reorganization of the debts of municipalities (which includes cities and towns, as well as villages, counties, taxing districts, municipal utilities, and school districts). A Chapter 9 debtor proposes a plan of adjustment of its debts, which allows the municipality to modify existing contractual obligations.

96. *See* 11 U.S.C. §§ 701–84 (2012) (Liquidation). Chapter 7 of the Bankruptcy Code provides for "liquidation," (i.e., the sale of a debtor's nonexempt property and the distribution of the proceeds to creditors). Upon distribution of such proceeds, the debtor receives a discharge of its obligations to creditors. To qualify for relief under Chapter 7 of the Bankruptcy Code, the debtor may be an individual, a partnership, or a corporation or other business entity.

97. *See* 11 U.S.C. §§ 1101–74 (2012) (Reorganization). Chapter 11 of the Bankruptcy Code generally provides for providing for reorganization. Typically, a debtor in a Chapter 11 case is a corporation or partnership. But individuals may also seek relief under Chapter 11. A Chapter 11 debtor usually proposes a plan of reorganization to keep its business alive and pay creditors over time, and receives a discharge of obligations other than as provided for under the plan of reorganization.

98. *In re* Jefferson Cty., 465 B.R. 243, 293 n.21 (Bankr. N.D. Ala. 2012).

Although the City's bankruptcy case will likely not reach any final resolution for many months, perhaps years, it is possible to outline several potential outcomes as they relate to the future of the DIA collections. The Attorney General's broad exemption of the DIA collections from sale or monetization is unlikely to be upheld. That means that the City will need to find a way to utilize the value of the DIA's collections in order to reach a feasible and confirmable plan of adjustment.[99] Short-term and long-term loans of certain of the DIA's artworks, the pledging of certain artworks as collateral for loans to the City, and the de-accessioning and sale of certain artworks will all be considered. Recent discussions have focused on finding what the federal judge appointed by the bankruptcy court to lead a mediation team has described as "a creative solution." Under this "creative solution," nine foundations "including Kresge, Hudson-Webber, Mott, Knight and the Ford Foundation of New York . . . [would] create a private fund to do two things: help the city honor pension commitments to its public-sector employees and protect the DIA and its valuable pieces from liquidation." In exchange, "the DIA and its assets . . . would be conveyed to a nonprofit charitable trust to ensure they never are imperiled again."[100] Whether or not this fund proposal moves forward, it is clear that the ultimate resolution will be a negotiated resolution, and it will likely include a significant political component.

99. The valuation and plan treatment of the DIA's collections are likely to be sharp points of contention as the city's plan process moves forward. Creditors will want to expand their role in the decision-making regarding the DIA's future. On November 26, 2013, an ad hoc group of creditors filed a motion asking the bankruptcy court to appoint a committee of creditors and interested persons to meet with the city "to assess the value of the [DIA's collections] based on arms-length market transactions that are consistent with recommendations regarding value-maximizing strategies made by and subject to consultation with a leading art intermediary or intermediaries. This collaborative process will enable the city and creditors to explore a wide range of options to monetize the [DIA's collections], including options that preserve the DIA as a culturally relevant institution as well as enhance creditor recoveries, in order to reach a consensus about the treatment of the [DIA's collections] under the plan." Motion of Creditors for Entry of an Order Pursuant to Section 105(a) of the Bankruptcy Code Appointing and Directing the Debtor to Cooperate with a Committee of Creditors and Interested Persons to Assess the Art Collection of the Detroit Institute of Arts Based on Arms-Length Market Transactions to Establish a Benchmark Valuation at 3, *In re* City of Detroit, No. 13-53846 (Bankr. E.D. Mich., filed Nov. 26, 2013), ECF No. 1833, *available at* http://www.freep.com/assets/freep/pdf/C42156391126.PDF.

100. Daniel Howes et. al, *Donors Pitched to Aid DIA, Pensions*, DETROIT NEWS (Nov. 14, 2013), http://www.detroitnews.com/article/20131114/METRO01/311140048.

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