Consignment Fraud – Keeping on top of your asset

Art can be highly valuable and is readily saleable; it has also traditionally been transacted with the minimum of formality. This gives rise to a high risk of fraud. This article examines one specific type of fraud: consignment fraud, describing what it consists of, giving some recent examples as well as suggestions as to what can be done to mitigate the risk.

What is consignment fraud?

It is common practice for people selling works of art, be they artists or purchasors of the works, to consign them to a gallery or other agent for them to be sold on the seller's behalf, typically on the basis that the seller pays a percentage commission. In the case of such consignment, the consignee – the person to whom the works are consigned – holds the works as an *agent* of the person selling them. This means that, in law, the consignee has the power to deal with the works, to sell them and receive the money for them.

In the law of England and Wales, anyone buying works of art (or any other goods) from an agent will own them as soon as the money is given to the agent – even if the agent never gives the money to the owner. This is different to the situation where the item is simply stolen, where the original owner retains legal title and can then seek to recover the item from a wholly innocent purchasor from the thief.

A consignor (a person consigning works of art to a gallery or similar) can therefore be vulnerable to fraud by the consignee, whereas purchasors may be less vulnerable in this situation. The consignor in such a case has a remedy for the missing money from the consignee, but this remedy is of limited practical usefulness if the consignee disappears without trace or has spent all the money and has no significant assets (and works of art held on consignment for others, or short leases of gallery premises, are not significant assets).

Some recent examples of consignment fraud

The Superior Court of Justice in Ontario has recently given judgment in a case of consignment fraud (*White Distribution v. Goring* [2018] ONSC 2333). In that case, the consignee, Goring (a Gallery owner), approached the consignor, White (a wholesale art supplier) in 2012, offering to sell some paintings owned by White on commission. White agreed, and 35 paintings were consigned.

By 2014, Goring had not reported the sale of any of White's paintings. In July of that year, White learnt that Goring's gallery was to close, and sought to retrieve his paintings. However, 22 of the 35 paintings were missing. The court described Goring as having "no reasonable explanation" as to what had happened to the missing paintings, estimated to have been worth CA$170,000. The Court awarded White

$170,000 in damages (plus $10,000 punitive damages and $7,500 in costs); but whether Goring has any money with which to pay White this sum is not apparent from the judgment.

Another example was reported in 2014 by an Arizona newspaper. In that case, a general "consign and design" shop in Phoenix closed after apparently having defrauded its customers. A local resident had consigned valuable paintings to the shop, estimated to have been worth US$350,000. The shop's owner initially told her that he had a buyer for the paintings, but later stated that they were worthless forgeries and that they had not been sold. However, when the owner attempted to collect them, she was told that the owner was not available and the paintings were never returned to her. When the shop closed, the paintings were not among the shop's stock. The same article reports that a similar situation had occurred in Arizona in 2010 with a different chain of consignment stores which had closed in that year after a criminal investigation. It is not clear whether any of the victims were ever compensated.

A well known case is that of Lawrence Salander, the operator of an art gallery in New York, which filed for bankruptcy protection in 2007 after failing to pay substantial debts owed to consignors (including the famous tennis player John McEnroe). He was convicted of grand larceny in 2010 and sentenced to between 6 and 18 years' imprisonment.

Salander, whose gallery was said by the Robb Report to be the "best in the world" in 2003, was found to have sold works consigned to him without telling the owners or paying them any money, lying repeatedly when asked for explanations, purportedly selling works that had not been consigned for sale, selling shares in paintings that had already been sold, and all the while using the money misappropriated to live a lavish lifestyle involving private jets and moving the gallery to a large mansion with velvet walls, a marble clad foyer and a monthly rent of over US$150,000 – far beyond what the gallery's actual sales could ever have supported.

Some practical tips as to how to minimise the risks of potential consignment fraud

To start to minimise any potential risks where artwork is consigned, a consignor should have a detailed contract with the consignee. The contract should set out clearly the terms of the consignment and make clear that the consignor has legal title. Although this will not allow works to be reclaimed from innocent third party purchasors, it will make it much easier for the consignor to quickly recover works retained by a consignee should any problems become apparent.

Consignors should make sure that they have registered their title or interest in the artworks with a database service such as ARTIVE.

A consignor should also make regular checks on the gallery to make sure the works are still with the consignee.

There can be non-dishonest situations where a long time passes, where artworks have been left in gallery stock rooms and staff move on and it is no longer clear that there is a consignor who owns the artwork. The artworks may simply get absorbed into the gallery's stock.

Keeping good records, such as a diary, to check regularly on progress of any potential sales of the art and to record who the consignor is dealing with at the gallery, should help a consignor to be aware of any problems at the earliest opportunity. This is significant where they may be a high turnover of staff at the gallery and therefore new staff may have little recollection or no knowledge at all about the consignor.

Consignors could also use security devices to protect their artworks, such as an electronic tag or other such security features that would allow tracking of their artworks. This would help to make it clear when the works have been removed from the gallery and might alert the consignor early to any problem.

In cases of fraud, a common feature is that the fraudster, knowing that he or she will eventually be caught, spends the money stolen on a lavish lifestyle, and thus has nothing left to pay creditors when the fraud is detected. There may also be various dishonest excuses given as to why the consignor cannot view her or his artworks or as to the position regarding sales or location of the art to conceal the true position from the consignor.

The works consigned are, after all, the consignors' assets and their responsibility to be completely on top of the situation, so problems can be detected at the earliest opportunity and prompt action can be taken.

Any situation in which – no matter what the excuse given – it is not possible for a consignor to view at short notice a work which the consignee states that he or she has not sold should be viewed with the greatest of suspicion, and urgent consideration should be given to obtaining an order freezing all of the consignee's assets (consult lawyers in the jurisdiction in which the consignee is located first).

The sooner that this be done, the less chance that the consignee will have to dissipate those assets in the first instance and the better the prospects of the consignor recovering some or all of them.

For any further information on issues of this type, please do contact us at the Art Due Diligence Group and for any legal advice or enquiries please contact us at 36 Art at The 36 Group.

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