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*although not directly within our goals, this article provides useful insights into the Art Market.

Case Review: Red Rothko Suit, a.k.a. Hoffman v. L&M Arts (TX)

Mark Rothko, Untitled (1961). Source: http://www.wikiart.org.

By Chris Michaels, Esq.*

A private art sale involving a Rothko painting is the subject of a bitter lawsuit in the Northern District of Texas. Inadvertently, the dispute sheds light on the often hidden intricacies and nuance of confidential deals.Hoffman v. L&M Arts, et al, deals with an alleged breach of contract relating to a confidentiality provision of a Letter Agreement that provided for a private sale of artwork. The lessons to be learned from this controversy may protect future sellers and buyers who may wish to enter into private sale agreements.

The painting at the heart of the sale is a 1961 Mark Rothko oil, *Untitled*, executed in bold red and orange (hereinafter the "Red Rothko"), which was owned by the Plaintiff, Marguerite Hoffman, a prominent art collector from Dallas. Plaintiff and her late husband pledged to donate their collection to the Dallas Museum of Art upon their death, although they retained the option to sell paintings during the lifetime. The Red Rothko was on loan to the Dallas Museum of Art, of which Ms. Hoffman is a trustee, prior to the sale, and Hoffman made a conscious decision to use a private sale option to safeguard from the public her decision to dispose of the work instead of donating it to the museum. In April of 2007, Hoffman sold the painting under the terms of a Letter Agreement, which served as an agreement between the Greenberg Van Doren Gallery acting for Hoffman and L&M Arts, a California gallery that has since closed, acting on behalf of the buyer. Principals for the Van Doren Gallery and L&M Arts signed the letter, which contained the following confidentiality provision: "[a]ll parties agree to make maximum effort to keep all aspects of this transaction confidential indefinitely. In addition, the buyer agrees not to hang or display the work for six months following receipt of the painting." Contractual agreements between Hoffman and Van Doren Gallery and between L&M Arts and the buyer, David Martinez are still confidential. But for the resulting controversy, the terms of the sale as well as the sale itself would have remained hidden from the public.

According to the complaint filed by Hoffman in May of 2010, the private April 2007 sale was finalized for a total price of $17.6 million. Subsequently, L&M invoiced David Martinez and Studio Capital, Inc. (also defendants in this case) for the painting. Studio Capital thereafter took possession of the painting and put it in storage. Three years later, the painting was consigned to Sotheby's for sale, and on 12 May 2010, the painting was sold at auction with great publicity for $31,442,500. The Hammer price exceeded Hoffman's earnings from the private sale by $13,842,500. As a result of the sale at auction, Hoffman brought suit against L&M, Martinez, Studio Capital, and others, alleging, among other things, that the defendants breached the confidentiality clause of the Letter Agreement and that subsequently Hoffman suffered damages because, "when she sold the Rothko painting privately, she did so at a substantial discount in exchange for the promise of strict confidentiality, forfeiting the additional millions of dollars the painting would have brought if sold at public auction." The

great chagrin and displeasure of Hoffman is easy to understand but whether her position has legal basis was left to the courts to decide.

In the December 2013 trial that followed, the jury found that the defendants did, in fact, breach the contract and awarded damages of $1.2 million to Hoffman. (The damages award itself presents a thorny procedural issue that will not be explored here). After the award was entered on behalf of Hoffman, all defendants moved for judgment as a matter of law, meaning that defendants were of the opinion that no reasonable jury could have found for the Plaintiff based on the available evidence. Of particular note for the purposes of this article, Martinez and Studio Capital, the buyers in the private sale, moved for judgment on the ground that a reasonable jury could not have found that L&M was either acting as their agent or that they were bound by the Letter Agreement. Essentially, Martinez and Studio Capital argued that they could not breach the confidentiality provision of the Letter Agreement because they were not bound by the Agreement in the first place, or were even aware of its existence.

In reviewing the Martinez and Studio Capital motions, the U.S. District Court for the Northern District of Texas, Dallas Division was faced with two issues: 1) whether there was legally sufficient evidence for a reasonable jury to have found that Martinez and Studio Capital conferred actual authority on L&M to enter into the Letter Agreement on their behalf; and 2) whether there was legally sufficient evidence for a reasonable jury to have found that L&M had apparent authority to enter into the Letter Agreement on behalf of Martinez and Studio Capital.

The Court, analyzing Texas law on actual authority, noted that "[a]n agent's authority to act on behalf of a principal depends on *some communication* by the principal either to the agent (actual or express authority) or to the third party (apparent or implied authority)." (Emphasis added). With respect toapparent authority, the Court noted that "one seeking to charge the principal through apparent authority of an agent must establish *conduct by the principal* that would lead a reasonably prudent person to believe that the agent has the authority that he purports to exercise." (Emphasis added).

Martinez and Studio Capital argued that L&M had neither actual nor apparent authority to enter into the Letter Agreement on their behalf. Regarding actual authority, the defendants maintained that L&M acted merely as an intermediary in purchasing the painting. Testimony by Martinez and the Principals of L&M backed up the argument that L&M was never authorized to sign the Letter Agreement on behalf of Martinez or Studio Capital. Hoffman presented several arguments in favor of finding that L&M had actual authority to act as the agent of Martinez and Studio Capital, including that the Letter Agreement itself stated that L&M was acting "on behalf of the buyer."

On the issue of actual authority, the Court found in favor of Martinez and Studio Capital. Simply put, the Court reasoned that there was no evidence that Martinez or Studio Capital *directly communicated* to L&M that it had authority to enter into an agreement with Hoffman that would be binding on either Martinez or Studio Capital. Additionally, the Court agreed with testimony of one of the Principals of L&M, who maintained that for private sales such as these, there are typically *two transactions* taking place; one between the seller and the intermediary and one between the intermediary and the buyer. The Court held that a reasonable jury could not find that either Martinez or Studio Capital communicated to L&M or otherwise implied through its conduct that L&M was authorized to enter into a contract with Hoffman that would be binding on the defendants in perpetuity and impose limits on their rights to alienate their property.

On the issue of apparent authority, the Court ruled that, in order to be liable, Martinez and Studio Capital must have engaged in conduct that reasonably led Hoffman to believe that L&M had this authority. The Court further noted that because neither Martinez nor Studio Capital had any direct interaction with Hoffman or her agent, among other reasons, the evidence did not permit the jury to have found that the defendants held L&M out as their agent. As such, the Court granted the motions of Studio Capital and Martinez and dismissed Hoffman's claims against them with prejudice.

As of 2 February 2015, the case is still active given that Attorneys for Hoffman appealed the latest ruling dismissing Hoffman's claims against the purchasers of the Red Rothko. There are, however, already a few important takeaways of which buyers, sellers, and dealers should be aware. One is that sophisticated buyers should be very clear with their dealers and intermediaries who purchase artwork as part of a private sale. An agreement in writing with respect to what the dealer is authorized to do, or not do on behalf of the buyer would, in light of the above case, be prudent. Additionally, buyers should be considerate of what they communicate or promise to a seller in private sales.

Hoffman is represented by Willkie Farr & Gallagher LLP, L&M Arts is represented by Susman Godfrey LLP, and Studio Capital is represented by Cleary Gottlieb Steen & Hamilton LLP.

Sources:

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