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1-29-2014

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Cardozo Arts & Entertainment Law Journal

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Recommended Citation
Day, Gregory, "The Economic Puzzle that is the Art Market" (2014). *AELJ Blog*. 33.
https://larc.cardozo.yu.edu/aelj-blog/33

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The Economic Puzzle that is the Art Market

Posted on January 29, 2014

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The manner in which buyers, sellers, and dealers conduct art transactions appears, at least initially, to contradict established economic principles. This blog post seeks to identify and illustrate this phenomenon using examples from the art attribution process. Indeed, the possibility that a purchased work was once forged or wrongly attributed threatens the value of many art transactions—and even more troubling is that the current legal framework seldom is able to provide relief and has, in many situations, even created market failure. As will be demonstrated, the result has been a type of market inefficiency that runs contrary to marketplace principals.

In short, most markets when left unregulated maximize collective wealth and produce a net sum of social benefits, but on occasion, markets can create harmful externalities and/or poorly distribute resources. Incidents of "market failure" should not last long though, considering that a number of actors—including buyers, sellers, voters, and local officials—all have incentives to remedy inefficiency. Given this background, why has the art market been fraught with inefficiency, yet remained so stable?

Three overwhelming problems potentially undermine an art transaction: one can rarely know for certain whether a work is worth the value paid, whether it has ever been stolen, or whether it has been properly attributed (or even forged). For instance, the process of attribution alone implicates several complex issues. Consider that evidence regarding who originally authored many older paintings has often been long lost, creating gaps in its provenance. Another similar problem arises when an artist's "school" or, in the case of Andy Warhol, "factory" produced the piece as standards and opinions vary about to whom a piece should be credited when more than one hand painted it. Further, highly skilled artists have created a number of works that mimic pre-existing pieces, *i.e.,* forgeries. Even if a work is legitimate, questions posed by experts about a work's authenticity can likewise, create a cloud over its title; several lawsuits have alleged that experts damaged a work's marketability when they rendered a negative finding regarding its authenticity.

This state of affairs has been exacerbated by the way the current legal regime hinders experts from adequately settling attribution disputes. Investigating the authenticity of a work is often difficult and costly considering the degree that a purchaser must rely upon experts. This is made even more cumbersome by the legal liability that threatens those brave enough to offer an opinion. Because many experts have been sued for product disparagement or defamation of title after asserting that a work is inauthentic, those buyers who desperately need expert advice often cannot obtain it from litigation weary experts. Art experts have also been known to work for the dealer, which may encourage an affirmative finding of authenticity despite evidence suggesting otherwise. Others have accused experts of finding against authenticity in order to drive up the value of their personal collections. In sum, determining the authenticity of a work is quite difficult, which is further frustrated by the fact that many of those best able to provide reliable information refuse to do and others may be providing information of a poor quality.

In turn, how should the law treat transactions involving a high-quality forgery? What if the seller had no knowledge of the work's lack of authenticity? Confusion often arises when several innocent parties have bought and sold the forged work at the price of an authentic work. Which party should bear the lost value between its purchase price and its current value: the current owner, the original seller, or some party in between? If the discovery of a forgery comes to light years or decades after its last purchase, the question becomes when the law should estop a purchaser from bringing suit. Since no one general legal rule has emerged, who bears the risk of loss often depends upon the state in which the conflict arose.

This blog post posed the question of why the above state of affairs should persist, as those who would benefit from increased efficiency should be expected to advocate for and effectuate some level of change, regulation, and/or supervision. My forthcoming research explains in greater detail that markets for goods, such as the art trade, can exist in a state of market failure if the preferences of the buyers and sellers are aligned, frustrating the virtues created by arm's length dealing. The article then endeavors to show that this dynamic has been created by the unique nature of goods that appreciate in value. Hopefully though, this blog post was able to illustrate the greater economic puzzle of the art market that has rarely before been discussed.

To read the full article, or other works by Gregory Day, please access his SSRN account.