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On the Law and Economics of Arts: A Research Proposal

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ABSTRACT: Arts is as old as humankind and a worldwide phenomenon. A scientific investigation of arts, however, is rather seldom since the arts are oftentimes applied and touch on multiple disciplines. Arts production and consumption are perceived as less rational and tangible than classic goods and services. Neoclassical economics therefore hardly has any account of the commercialization of arts. The opening of the neoclassical economics model for behavioral aspects in the behavioral economics revolution has now paved the way to start researching the arts and surreal pricing mechanisms in the arts world. This paper is a call for research of arts from a Law & Economics perspective. Law & Economics offers ways to understand the value of arts in society and derive inferences on how to improve certain features and peculiarities of the arts market. A Behavioral Law & Economics perspective could help elucidate social welfare enhancement potential for the individual passive consumer of arts, the active arts market actors as well as economies and society as a whole, including future generations. With the growing commercialization of arts and rising use of arts as an unregulated collateral in the finance world, capturing the peculiar dynamics of arts markets holds unprecedented value. Legal recommendations could target at addressing market downfalls and risk management strategies in the arts world.

KEYWORDS: arts, behavioral economics, commercialization of arts, cryptocurrencies, culture, non-fungible token (NFT), private goods, public goods, tickets, tokens

Introduction

Arts is as old as humankind and a worldwide phenomenon. A scientific investigation of arts, however, is rather seldom since the arts are oftentimes applied and touch on multiple disciplines (Ginsburg and Throsby 2006). Arts production and consumption are perceived as less rational and tangible than classic goods and services (Baumol and Bowen 1966). Legal considerations of the arts are usually only focused on peculiar art segments (Guerra-Pujol 2019), specific rights (Hansmann and Santilli 1997; Rushton 2001) or specific time periods (Piano and Piano 2023). To this day no scientific account exists of the growing contemporary connection of arts and finance, especially with a digital focus. Neoclassical economics therefore hardly has any account of the commercialization of arts. The opening of the neoclassical economics model for behavioral aspects in the behavioral economics revolution has now paved the way to start researching the arts and surreal pricing mechanisms in the arts world. The proposed research is targeted at direct (economic) implications for managers and practitioners.

In the most recent decade and years, the commercialization of arts has progressed due to several trends. Since the 2008/09 World Financial Recession led to a regulation of volatile market segments, such as the U.S. housing sector, arts have become the new unregulated collateral in economies around the world. The advent of cryptocurrencies has also opened opportunities to a new unregulated market to capitalize online from non-fungible token (NFT) art. The COVID-19 pandemic has driven the trend of online arts production and consumption as an alternative to conventional gateways. After a limited and long-suppressed live arts consumption possibility during the pandemic, the demand for arts tickets has skyrocketed driving the event ticket secondary markets to unprecedented highs. Places like Monaco, which features the highest density of those who became rich with arts, have benefited from enormous economic growth in recent years – for instance, Monaco experienced between 11-21% GDP growth in the years 2021 and 2022. Financial investors more and more tap into the arts world and artistic market capitalization, if one considers investors having turned to influential arts dealers like Jeffrey Koons – who rose from being a financial investor to the highest paid contemporary arts producer, oftentimes critically referred to as art broker, in the world.

All these novel trends demand for a closer investigation of the law and economics of arts, which has not been covered in scientific investigations so far. This research proposal advocates for investigating arts from a Law & Economics perspective in order to understand the value of arts in society and derive inferences how to improve certain features and peculiarities of the arts market. A Behavioral Law & Economics analysis could elucidate social welfare enhancement potential for the individual passive consumer of arts, the active arts market actors as well as economies and society as a whole, including future generations. Legal recommendations could also be derived that target at addressing market downfalls and risk management strategies in the arts world. Emphasis is given to studying the economic value creation of arts from a comparative angle and historical foundations perspective, given the arts' long history of royal courts competing over arts production that has created artistic output that – to this day – generates substantial economic value in the form of attracting incoming tourism.

Open research questions

In what way do the arts resemble and in what features does art deviate from normal goods and market dynamics? How does law secure arts markets, with particular attention to the digital world? How does economics capture arts markets? What behavioral economics effects come to play in (digital) arts markets? What can Law & Economics analyses offer to improve arts markets? Should the NFT-cryptocurrency art markets and online secondary market art sales be regulated and if so, how?

Preliminary insights

The commercialization of arts in the digital age

Since the advent of the internet, the commercialization of arts has change in the digital sphere. The COVID-19 pandemic has driven the trend of online arts production and consumption as an alternative to conventional art market gateways. After a limited and long-suppressed live arts consumption possibility during the pandemic, the demand for arts tickets has skyrocketed driving the art event ticket online secondary markets to unprecedented highs. One of the newest trends in the commercialization of arts is the advent of cryptocurrencies as an unregulated market to capitalize from online non-fungible token (NFT) art.

A Law & Economics cost-benefit analysis of digitalization of arts could show the enormous potential (e.g., democratization of arts by paying royalties long-term) but also the risks (grounded in heterodox surreal price mechanisms and regulation leaping behind market developments as well as rising market capitalization of arts).

Competition in Arts in the Digital Age could cover the Law and Economics of Arts online from a Competition Law for New Business Models angle. The Introduction will start with a snapshot of the basic knowledge of the methodology of the economic analysis of digital markets law and of the microeconomic analysis of the functioning of online markets. The Introduction will then cover a new angle of business competition law with particular attention to a heterodox economics extension of the traditional neoclassical approach. The Theory will apply heterodox Law & Economics insights to the case of new business models typical of the digital economy in the arts domain (Cooter and Ulen 2011).

The overall goal of this research would be to understand competition Law & Economics in the digital age for the arts market. Online platform competition dynamics of digital arts markets could be described with special attention to major legal issues raised with the advent of digital social media platforms (Baldwin and Woodward 2009) and the rise of digital ecosystems (Cennamo 2021). The legal background of data-driven digital companies in regard to online art business models and their specificities will become subject to scrutiny. A Law & Economics analysis of arts in the digital sphere will be conducted in order to detect the economic and legal issues that may emerge from arts market practices online. The critical assessment of the efficiency of the current body of regulation will help determine adequate regulation levels and propose concrete regulation to improve arts market dynamics in the digital age.

Digital online markets warrant for legal attention – especially when considering direct and indirect network effects, economies of scale and scope, lock-in effects, self-preferencing strategies, by default installation of apps and stores, as well as the role of interoperability. The newest trends in the online creation of arts will be discussed as well as the digital capitalization of arts analyzed. Comparative Law & Economics benefit and cost analyses of contemporary regulation will pay special attention to competition and oligopolies (Petit 2020).

Future research could set out to understand the Law & Economics arts in digitalized markets and derive inferences how to improve certain features and peculiarities of the digital arts market. Concretely NFTs could be captured as different market strategy as royalty payments can be enacted over time and easier than in the traditional literary market. The concrete application of Law & Economics theories for Arts production in digital contexts will indirectly test the usefulness but also reveal the limits of various strands of Law & Economics analyses in the digital age.

The value of arts over time

When analyzed from an economic perspective, art can be a public and private good with enormous and unique long-term value potential. Future research could integrate another temporal dimension of discounting payoffs in the standard public vs. private good quadrant with rivalry and excludability as dichotomous axes. For instance, standard consumer goods usually have a clearly defined depreciation (e.g., car 6 years, house 20 years) and then their value is 0 for insurances. Public goods often have longer-term depreciation (e.g., a highway or bridge usually lasts for a decade until it has to be renewed). 95-99% of created art has limited value after production, but about 1-5% become more and more valuable over time.

There are no solid studies, which art is successful and why. But it may be connected to a temporal element and being the first one to capture a trend but also to grant unique value to society. We see this in some arts pieces that they sustained centuries for granting some unique value to society, even it that value at a certain point is only derived from being an anachronism that tells about past life and living conditions (e.g., Neanderthaler cave drawings or broken stone pieces in Egypt). If certain art makes the cut to be the 1-5% remaining artifact of a certain time, then the value seems to increase over time -- even for wrong pieces that add no value (e.g., why are we still citing Adam Smith's Wealth of Nations, discussing fundamentally wrong books that incited war, etc.). Why does some art make the cut to become a classic, while other work disappears? What will digitalization do to these dynamics? If long-term value creation of arts is possible, why does society often not remunerate future-oriented artists but has an implicit incentive that artists die young (so an ultimate cap ensures finite scarcity) and their art is subject to crime (gets stolen or looted) to attract media attention? And how does the Keynesian multiplier theory capture all different categories of goods (likely consumer goods consumption having the lowest multiplier effect, public goods creation a larger multiplier effect and maybe arts production the largest multiplier dependent on the survival of art)? Are just a few preliminary questions that may be asked and hopefully answered in this section.

Behavioral Economics of Arts

To this day, there is no specified classification of arts in economics. Art markets tend to have their own, eccentric economic features. The surreal price mechanism of the arts and in almost all forms of art, only a very small fraction is extraordinarily lucrative but unlike in other high-stakes markets, the laws of success in the arts world appear less tangible, transparent and predictable.

The planned behavioral part will feature peculiarities of arts markets like price anomalies in the arts. There is a price spike in the aftermath of criminal activities in arts markets. For example, Nazi looted art or Leonardo da Vinci's Mona Lisa having been stolen in 1911 or Cellini's Saliera having been stolen in the early 2000 experienced a price spice due to the media attention that came with crime.

Another behavioral economic pricing anomaly in the arts is due to the detrimental price value extraction of suffering artists in the creation of arts (drugs, eccentric behavior, childlessness of ballet dancers, lack of self-care...) setting wrong incentives in the selection and care for artists by art brokers, managers, gatekeepers. In addition, there is a surreal price spike when artist dies (likely for having reached the ultimate cap of unique production pool turning specific artwork into an ultimately finite scarcity good), which exacerbates if the death is tragic, self-inflicted, young and unexpected. Art markets are relatively unregulated and if intertwined with finance, art markets appear to offer shadow operations. For instance, there is a European central bank that had a Stradivari as collateral, which simply disappeared on sight. The bank managed to write it off without public scrutiny.

Art sales in auctions have been criticized for being non-transparent and lacking appropriate legal means to control the contemporary conduct. For instance, there is the phenomenon of 'Chandelier bidding' in live auctions, where the bid collector points at the chandelier and pretends there was a bid, when there was none, in order to raise prices in an auction price race to the top. There are repetitive news pieces out on information asymmetry and insider trading in arts markets as well as art brokers stealing ideas and labor from young artists but no clear account and code-of-conduct exists how to regulate such inefficient and/or unethical market conduct.

Since art pricing is perceived to be less tangible, consumer protection and market oversight appear to be less stringent than in other industries. There are also some unpredictable surprising elements in the arts market that seem to counteract regular market behavior, e.g., if a mistake is made on an artistic stamp that can bestow extraordinary value.

Art is a connoisseur market, in which consumers need to build up knowledge on their own to avoid being offered an unfair price, e.g., when thinking about per centimeter prices of painting artists used as non-refined overall measure for an artist's overall markt value, which allows to sell cheap drafts for an unsubstantiated higher price to uneducated art buyers.

Heterodox price theory outlines how bubbles form in an expected value rising above the fundamental value due to market buzz about an upcoming product or trend. When financial leaders and in the following too many following finance market participants realize that the expected value is too elevated from the fundamental value of a good, prices drop and bubbles burst. This heterodox price theory has not been captured for arts markets or the NFT market, where different dynamics, information transfer regimes and network effects as well as different liability claims mechanics may come to play.

While arts markets are praised as a good investment that tends to hold value over time and appears to be more independent from cyclical general market fluctuations, a new trend of the rising commercialization of arts online now challenges the robustness of arts as a stable market option and collateral, which may impose systemic risks if the market capitalization of arts rises to a substantial level.

Research agenda

First, the arts will be classified in different categories. Then, the different forms of arts will be reflected upon the standard scheme of public and private goods and the unique long-term value creation by the arts for society outlined. Arts will be investigated from a behavioral economics standpoint and surreal pricing mechanisms in the arts uncovered with attention to ethics and corporate social responsibility. While the old source in the literature will be acknowledged as relevant advent of Law & Economics studies of the art, the contemporary discussion of arts and economics will then embark on a broader analysis.

The newest trends in the online creation of arts will be discussed as well as the digital capitalization of arts. NFT art markets' democratization of arts value through continuous funding options for artists will be discussed in a legal analysis. NFT arts markets' features to be volatile and implying risks of sudden corrections to fundamental values, which implies risk in the case of digital art as unregulated collateral in the finance world, will be analyzed from an economic perspective. A cost-benefit analysis of the capitalization of arts as collateral with short-term, medium-term and long-term focus and risk prospects will be provided to inform politicians, policy makers and global governance executives. Overall, the research will also compare and contrast the public sector versus private sector arts creation based on historic examples (e.g., European royal courts) as well as contemporary approaches to digital art in Europe and North America (e.g., art tokens, art collaterals, financial executives as art brokers, online secondary markets).

As legal scholarship has limited account of regulatory improvement of the arts market and with the advent of an intertwined arts and finance market as well as art as an unregulated collateral, attention must be drawn to different regulatory attempts to regulate prices and supply-demand relations in the arts markets. Future research should aim at regulation in the arts market from a Law & Economics perspective. Special attention should be paid to new business models of arts in the digital world. Substantial questions on regulating art should be raised – such as the benefits of financial stability but also risks of crowding out creativity with regulation. A Law & Economics analysis of arts in the digital sphere will be conducted in order to detect the economic and legal issues that may emerge from arts market practices online. The critical assessment of the efficiency of the current body of regulation will help determine adequate regulation levels and propose concrete regulation to improve arts market dynamics in the digital age.

Future research questions could address if arts markets would benefit or be burdened by regulation? What are international approaches to regulate art? What are concrete areas of demand for regulation in arts production and consumption online? How do platform-powered eco-systems change the arts markets with particular attention to pricing, building trust, privacy, discounting and stakeholder balancing?

The rising connection between arts and financial markets should be covered in descriptive empirical analyses. The newest trends in the online creation of arts could be discussed theoretically as well as the digital capitalization of arts descriptively analyzed. Comparative Law & Economics analyses will highlight different country approaches to regulate art pricing.

Prospective output

Overall, arts markets will be discussed in order to determine what features of digital online markets warrant for legal attention. Investigating the arts from a Law & Economics perspective promises to grant most novel insights into a growingly-commercialized economic good that has mainly been left out of scientific investigation of finance and economics. A new nomenclature of arts in light of the classic public and private good dichotomy will enable to underline the unique value of arts for society. The behavioral economics angle can unravel ethical downfalls and hurtful incentives in the creation of arts, which allows for improving the working conditions and wellbeing of artists as well as the economic productivity of arts markets. Addressing the most recent capitalization of arts in the digital world serves historic purposes in capturing the advent of a new form of arts as well as allows for closing dangerous regulatory gaps that may impose implicit systemic market risks as well as societal welfare losses. Art as the unregulated collateral of our times will be discussed and its ramifications for society debated.

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