Auction Guarantees in the Contemporary Art Market

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I hereby certify that this master thesis has been composed by myself, and describes my own work, unless otherwise acknowledged in the text. All references and verbatim extracts have been quoted, and all sources of information have been specifically acknowledged. This master thesis has not been accepted in any previous application for a degree.

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1 Introduction

This master thesis analyses the auction house guarantees system in the context of the booming contemporary art market in the framework of the Executive Master in Art Market Studies. At recent auction sales, auction houses have been setting one auction record after the other. What is behind this? How is it possible that the art market is so optimistic and increasingly growing? Is there a bubble and for how long will these constant auction sales continue? And, what is the role of guarantees in connection with these questions?

Many factors are responsible for the increased prices gained at art auctions since 2007. There have been many articles in the recent press about auction house guarantees and especially on third party guarantees. Commentators have also looked at critical views in connection to the growing contemporary art market and guarantees as well as manipulation and transparency in the art world. Some argue that there should be more regulation in the art market, and the guarantees system is one of their target fields.

In this essay I look closely at guarantees and issues surrounding the guarantees system. Part one is theoretical. In this section I first make some general remarks and provide outlines of important terms; secondly I touch on the history of auction guarantees and legal structures; next I take a more detailed look at guarantees from the auction house perspective, especially in the case when the auction house acts as a guarantor; then I move to an examination of the seller's perspective and the collector's point of view, who is the third party guarantor in many cases. Finally, I analyse guarantees from the perspective of the buyers.

The second part contains a practical research exercise based on the available auction data. I take a closer look at how and why contemporary art developed to the most important art market sector. Then, I look closely at contemporary art auction sales over the last seven years and analyse sales and guarantees, current topics and developments and trends in connection to guarantees and the growing contemporary art market. Finally, several case studies illustrate various scenarios involving guarantees and show the outcome.

The sources used in this paper include publications, press articles, auction sales results and other publicly available information on the topic of guarantees.
While auction guarantees are a hot topic, there is little to no literature available on this topic for sale or in libraries. Furthermore, auction house experts were not easy to reach for an interview, largely because this topic remains a somewhat confidential practice at auction houses. Hence, the most important sources used in this paper were online press articles.

I am also very grateful to my supervisor Thomas Seydoux for his great input and help.

2 General

2.1 The Art Auction Market

The art auction market is dominated by two traditional auction houses, Christie's, founded in 1766, and Sotheby's, founded in 1744. These houses have a duopoly on the market and between them have a market share of 90% of the international art market.[1]

Historically, the privately owned auction house Christie's has concentrated on the sale of various art objects, whereas the publicly listed Sotheby's has been more involved in blockbuster sales. These have included the 1996 sale of the estate of Jacqueline Kennedy, which brought USD 34 million, and the 1998 sale of the estate of the Duke and Duchess of Windsor, which went for more than USD 23 million.[2]

"An old saw in the art world claims that the difference between Sotheby's and Christie's is that the former are businessmen pretending to be gentlemen and the latter are gentlemen pretending to be businessmen".[3] The auction house Sotheby's has been a publicly listed company on the New York Stock Exchange[4] since 1988, whereas Christie's is still in private hands, owned by the French businessman and collector Francois Pinault.[5]

Phillips holds the third place in the auction market. The rapid growth of this auction house is suggested as one of the reasons for the issuing of guarantees to clients by the two leading houses.

It is also worth remembering that there are numerous small auction houses, which are of regional importance to local markets.

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[1] Boll 2009 Dirk Boll, *Kunst in käuflich. Freie Sicht auf den Kunstmarkt*, Zurich, rüffer & rub Sachbuchverlag, 2009, p. 39.

[2] Rohleder 2001 Anna Rohleder, *Which Auction House Is Right For You?*, in Forbes, on 14 November 2001, http://www.forbes.com/2001/11/14/1114connguide.html, last access on 25.02.2015.

[3] Ibid.

[4] Sotheby's at New York Stock Exchange, https://www.nyse.com/quote/XNYS:BID, last access on 25.02.2015.

[5] Francois Pinault on Forbes.com, http://www.forbes.com/lists/2006/10/FUBG.html, last access on 25.02.2015.

Since 2007 there has been a huge expansion of auction houses in the direction of the contemporary art market.
Both Christie's and Sotheby's are very strong in the contemporary art market. According to the Art Tactic Outlook 2015 "the auction sales of contemporary art accounted for 46.8% (up from 44% in 2013) of the Sotheby's and Christie's overall auction sales of Chinese art, Old Masters, Impressionist and Modern and Post-War & Contemporary art."[6]

All three auction houses achieved record results in 2014. "Christie's, Sotheby's and Phillips' Post-War and Contemporary Evening Sales in New York and London raised in excess of USD 4.54 billion in 2014, more than 34% higher than 2013."[7]
According to the forecasters, Christie's is believed to become the best performing auction house in 2015.[8]

Another development in the auction market is the expansion of auction houses in the primary market, which traditionally belonged to galleries and art traders. Auction houses are opening various gallery spaces and hosting exhibitions worldwide.[9] The idea of the auction house opening such gallery spaces is to organize exhibitions and to encourage collectors to buy artworks through an auction house in a private sale.[10] Apart from exhibition activities, they also encourage collectors to consign artworks and make important contemporary art sales.

Further expansion is observed in online auction sales, which are predicted to develop even further. The auction houses see big potential in online auctions to attract younger generations of collectors. This year the online sales at

[6] ArtTactic Outlook 2015, p.3.
[7] Ibid, p. 3.
[8] Ibid, p. 2.
[9] Herchenröder 2015 Christian Herchenröder, *Der Kunstmarkt und seine Strategien: Immer höhere Umsätze,* in Neue Zürcher Zeitung, on 24 January 2015, http://www.nzz.ch/feuilleton/kunsthandel-auktionen/immer-hoehere-umsaetze-1.18467825, last access on 25.02.2015; Sotheby's Gallery, http://www.sothebys.com/en/gallery/exhibitions.html, last access on 25.02.2015; Christie's Exhibitions and Events, http://www.christies.com/events/, last access on 25.02.2015.
[10] Miller 2014 M.H. Miller, *Christie's Will Open New Galleries This Month Focused On Private Sales,* in ArtNews, on 3 November 2014, http://www.artnews.com/2014/11/03/christies-will-open-new-galleries-this-month-focused-on-private-sales/, last access on 25.02.2015.

Christie's have risen to GBP 21.4 million, which represents 2.4% of the total turnover.[11]

Another frequently used instrument, which is seen as one of the most powerful as well as controversial, is the guarantee. It is issued by the auction house to attract the seller to consign and will be examined closely below.

2.2 Definitions and the Idea Behind the Guarantee

"A guarantee is an agreement to pay a specified amount for a work, regardless of whether or not the work actually sells."[12] Guarantee is a financial instrument used by the auction houses to secure the supply of high valued artworks.[13] Auction houses use this instrument primarily for auction top lots, and consequently the parties involved are mega collectors or art market traders. Collectors can be moved towards consignment of an artwork, as they know that they will be paid independent of the auction result.

High valued artworks are lots valued at more than USD 1 million, which are of a certain importance or in great demand.[14] Furthermore, an auction house might propose a higher guarantee in order to stay competitive and to try to secure the consignment as the seller could otherwise choose another auction house.[15]

The amount of the guarantee is usually the lower auction estimate for the artwork.[16] However, the involved parties are free to arrange other solutions. Since 1993 Christie's has been indicating in its catalogue whether they have a financial involvement in a certain lot. This is in compliance with US law, which obliges it to mention whether there is such a financial interest.[17] All the guaranteed works have a special sign in the auction catalogues. Sotheby's includes an º and Christie's has an explanation at the end of the catalogue.

[11] Herchenröder 2015.
[12] Rozell 2014 Mary Rozell, *The Art Collector's Handbook. A Guide to Collection Management and Care*; Lund Humphries, Farnham and Burlington, 2014, p. 170.
[13] Boll 2009, p. 202.
[14] Lindemann 2006 Adam Lindemann, *Zeitgenössische Kunst sammeln*; Cologne, Taschen Verlag, 2006, p. 218.
[15] Ibid, p. 236.
[16] Boll 2009, p. 202.
[17] Mason 2004 Christopher Mason, *Inside the Sotheby's - Christie's Auction House Scandal*; New York, 2004, p. 109 and 140.

Furthermore, there is also a distinction between lots guaranteed by the auction house itself and a third party investor. This distinction has been visible in Sotheby's auction catalogues since 2008.[18] Christie's catalogues started to distinguish between in-house guarantees and the third party guarantees in 2010.

A consignor is guaranteed to receive at least the guaranteed amount – this is the idea behind the guarantee, which works as an insurance for the seller.[19]
In case the work sells for a higher price than a guaranteed sum, the auction house (in his position as the guarantor) gets the seller's commission, the buyer's commission and a portion of the upside, if it had been not arranged in the contract that the seller gets everything.[20] Ideally the auction house would first propose to the consignor to split the overage 50/50 taking into consideration the risk factor.[21] However, normally the seller and the auction house arrange that 30% of the upside goes to the auction house, and 70% to the seller/consignor. However, taking the level of the risk involved into consideration, it can happen that the auction house will pre-arrange to get a higher percentage of the upside.[22]
In the case of the third party guarantor, s/he gets a share of the buyer's premium. In this case the auction house gets the seller commission and the share of the buyer's commission. The upside will be divided between the seller, the auction house and the third party as per the guarantee clause. Normally the third party and the auction house arrange to split the 30% of the overage 50-50, which means that the consignor gets 70% and the auction house and the third party guarantor receive 15% each.

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[18] The Economist, *Financial machinations at auctions,* in The Economist, on 18 November 2011, http://www.economist.com/blogs/prospero/2011/11/art-market, last access on 20.02.2015.
[19] Adam/Burns 2011 Georgina Adam and Charlotte Burns, *Guaranteed Outcome* in The Art Newspaper, on 2 March 2011, http://www.theartnewspaper.com/articles/Guaranteed+outcome/23341, last access on 18.02.2015.
[20] Lerner/Bresler 2012 Ralph E. Lerner / Judith Bresler, *Art Law. The Guide for Collectors, Investors, Dealers, and Artists*; New York City, Practising Law Institute, 2012, p. 318.
[21] Thompson 2014 Don Thompson, *The Supermodel and the Brillo Box*; New York, Palgrave Macmillian, 2014, p.160.
[22] Mason 2004, p. 139.

In the case that the artwork remains unsold, the guarantor (auction house or a third party) will keep the artwork and pay the guaranteed sum of money to the seller. The auction house will still get the seller's commission and in the case of a third party guarantor, also the buyer's premium.[23]

In the case that the work sells for exactly the guaranteed price and the auction house is the guarantor, the auction house receives the seller's commission and the buyer's premium.
In the case that the guarantor is a third party guarantor, the buyer's premium will most probably be divided between the auction house and the third party guarantor as per their agreement.

The guarantee instrument is not very common in German-speaking countries.[24] Christie's and Sotheby's mostly use it during their blockbuster sales in New York and London.

2.3 Historical Overview of Guarantees

The history of the guarantees goes back to the 1970s when auction houses started to use this instrument to secure consignments. However, there are also documents that show that auction houses used similar instruments as early as the beginning of the 20th century.[25] Interestingly, the rise of the guarantee coincides with the time when art started to be seen as investment. The function of art as an alternative investment owes itself to the general expansion of the international art market, which increased interest on the collector's side.[26]
Sotheby's invented the auction guarantee in order to secure consignments from its competitor Christie's.[27] Sotheby's issued its first guarantee in 1971 to

[23] Lerner/Bresler 2012, p. 321.
[24] Sammler Seminar *Auktionen* in Weltkunst N°90, August 2014, p. 79.
[25] Horowitz 2011 Noah Horowitz, *Art of the Deal: Contemporary Art in a Global Financial Market*; New Jersey, Princeton University Press, 2011, p. 194.
[26] Wagner/Westreich Wagner 2013, Ethan Wagner and Thea Westreich Wagner, *Collecting Art for Love, Money and More*; London and New York, 2013, p. 78.
[27] Croisier 2014 Presentation of Jérôme Croisier, *Art Valuation* Lecture, Executive Master in Art Market Studies, Zurich, on 17.12.2014, p. 10.

secure the sale of 47 Kandinsky paintings from the Guggenheim Museum.[28] It seems that Sotheby's was the only auction house to use the guarantee for several decades. In 1990 Christie's was finally forced to use auction house guarantees in order to stay competitive.[29] It was a highly confidential practice of the auction house at the time.

The guarantees disappeared immediately after the oil crisis in the 1970s and came back in the 1980s when Japanese collectors entered the art market.[30]

In 1990 the art market collapsed and various guaranteed artworks remained unsold, which caused both auction houses to re-think their strategies and to take a more conservative approach to guarantees.[31] Due to the First Gulf war and the overall economic situation in 1990-1993, art prices fell by 55%.[32] From September 1993, both Christie's and Sotheby's stopped giving any "straight guarantees – the kind where the auction house did not get to share in the proceeds if the winning bid exceeded the guarantee price promised to the consignor."[33]

2001 is an important year in the auction house guarantees history as it marks the rise of the auction house Phillips, which was acquired by LVMH[34] owner Bernard Arnault. Arnault had hoped to bring Philips to the level of the duopoly auction houses Christie's and Sotheby's.[35] This eventuated in the Philips auction house guaranteeing USD 185 million for the sale of the Smooke Collection, which was estimated by experts to only be worth USD 80-100 million.[36] The final auction result was not far from the estimate bringing together USD 85 million. After the huge loss in guarantees (which is thought to be around USD 400 million) the auction house was sold to Simon de Pury.[37]

The peak of the guarantees business was during the financial crisis year of 2008. The auction houses experienced huge losses during the financial

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[28] Adam/Burns 2011.
[29] Mason 2004, p. 84.
[30] Croisier 2014, p. 10.
[31] Mason 2004, p. 85-86.
[32] Hernando 2015 Elisa Hernando, *Art Market Crisis?* in Art Pulse Magazine, 2015, http://artpulsemagazine.com/art-market-crisis, last access on 19.02.2015.
[33] Mason, p. 119.
[34] World-Leading Group in Luxury Products – Moet Hennesy-Louis Vuitton.
[35] Adam/Burns 2011.
[36] Horsley 2011 Carter B. Horsley, *Smooke Collection* in The City Review, on 5.11.2011, http://www.thecityreview.com/f01phsmo.html, last access on 18.92.2015.
[37] Adam/Burns 2011.

crisis, which forced them to stop giving auction guarantees.[38] Sotheby's lost about USD 52 million in just one season as it could not sell lots at the guaranteed price and had to pay the sellers.[39]

As of 2011 auction guarantees seem to have made a comeback, but with strategic change to the form of the third party guarantees. The "renaissance" of the auction house system is marked by several interlinking factors. These include the strong contemporary art market, the attempt by both Sotheby's and Christie's to secure the business of high valued top lots and the strong competition between both auction houses.

In 2014 "Sotheby's pledged to cover minimum prices on works that made up 43 per cent of the USD 422 million in revenue at its November Impressionist and Modern art sale, which is typically one of its highest-grossing auctions of the year. Christie's has moved in the same direction. At its post-war and contemporary art sale in November, it directly guaranteed 23 lots that accounted for 44 per cent of the sale's USD 853 million in revenue".[40]

2.4 Guarantee Types

2.4.1 General and Reserve Price

Auction house guarantees are usually of two types – direct guaranteed, which are secured by the auction house itself, and third party guarantees, which include a third party. After 2000 there was a shift from guarantees issued directly by the auction house to third party guarantees. The main reason for this recent development is the auction houses' strategy is to limit the risk to the minimum after several financial losses in the past. Hence, auction houses search for third parties who are interested in either possessing the object or making a deal.

[38] Heath 2013 Christian Heath, *The Dynamics of Auction. Social Interaction and the Sale of Fine Art and Antiques*; Cambridge, 2013, p.14.
[39] Bowley 2015 Graham Bowley, *Sotheby's and Christie's Return to Guaranteeing Art Prices* in New York Times, on 7 January 2015, http://www.nytimes.com/2015/01/08/arts/design/sothebys-and-christies-return-to-guaranteeing-art-prices.html, last access on 16.02.2015.
[40] Ibid.

A general distinction must be made between the guarantee price and the reserve price. The reserve price is set for every lot and represents a minimum price, which was pre-arranged and agreed on between the auctioneer and the consignor.[41] It is normally set at or below the lower estimate of the lot.

In comparison to the guaranteed work, if the reserve price is not met, the object will remain unsold in the property of the consignor and will become a bought-in.[42] Hence, the guarantee price can be seen as an exclusive and secured reserve price, as the lot will be sold even if the minimum (reserve) price remains unreached.

2.4.2 Irrevocable Bids

Apart from the term "guarantee", we also find the irrevocable bid in the auction guarantee system.

An irrevocable bid is a bid made by a person for an undisclosed amount prior to the auction sale taking place. "If no one bids any higher, then the buyer gets the work and pays the buyer's premium. However, the guarantor would be charged not a full, but a partial, lower pre-arranged buyer's premium.[43] If the work sells for more, then the "irrevocable bidder" gets a cut of what is called the "upside", the difference between the final price and the secret price he or she agreed to bid."[44] The first time a symbol for such a bid appeared was in the Sotheby's catalogue for its Impressionist and Modern sale in New York in 2008. The irrevocable bid was issued for Kazimir Malevich's *Suprematist Composition* (1916) estimated at USD 60 million.[45]

The irrevocable bid appears to go in the direction of the third party guarantee. However, the auction houses try to distinguish between the third party guarantee and the irrevocable bid, explaining that the third party guarantor is

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[41] Feldman/Weil 1986 Franklin Feldman / Stephen E. Weil / Susan Duke Biederman, *Art Law: Rights and Liabilities of Creators and Collectors*; Boston / Toronto, 1986, p. 92.

[42] Sotheby's Glossary, http://www.sothebys.com/en/Glossary.html, last access on 8.3.2015.

[43] Thompson 2014, p.163.

[44] Adam 2008 Georgina Adam, *The art market: All eyes are on antique* in The Financial Times, on 8 November 2008, http://www.ft.com/intl/cms/s/0/9d4b7422-ac59-11dd-bf71-000077b07658.html, last access on 23.02.2015.

[45] Ibid.

not entitled to bid, whereas the irrevocable bidder makes a bid during the auction on the guaranteed piece.[46]

This distinction has been discussed by experts, some of whom oppose this explanation by arguing that third party guarantors can and do also bid on guaranteed lots.[47]

The idea of remuneration within the irrevocable bid goes in the same direction as that of the guarantee. Sotheby's Annual Report contains the following information on irrevocable bids: "If the irrevocable bid is not the winning bid, the counterparty is generally entitled to receive a share of the auction commission earned on the sale and/or share of any overage."[48] In other words, the third party guarantor receives a kind of remuneration (share of commission or share of the upside) in the case that the lot sells over the sum of the irrevocable bid to a third party buyer.

Technically, there is no difference between the third party guarantee and the irrevocable bid and the distinction does not really make sense in terms of the outcome. According to my discussions with several art market specialists the investor is free to decide whether or not to bid over the guaranteed price during the auction itself.

In most cases third party guarantors are mega collectors and art dealers who control the market. When they do not want an artist who is important to them to drop the price or to be bought-in at the auction, they will take the role of the guarantor.[49] These art market players have a direct interest in the artworks selling for high prices.[50] As such, the third party guarantor has a certain power of manipulation.

Such an art investor has a powerful position as s/he is entitled to receive extra information and is allowed to bid in order to increase the price.[51] Currently, guarantors at both auction houses are allowed to bid. The explanation behind the right to bid is that a guarantor is not an owner (who is

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[46] *Sotheby's irrevocable bid explained*, 12.11.2008, http://artradarjournal.com/2008/11/12/sothebys-new-irrevocable-bid-explained-ft-saatchi/, last access on 19.02.2015.

[47] Lerner/Bresler 2012, p. 322.

[48] Sotheby's Annual Report 2013.

[49] Lindemann 2006, p. 219.

[50] DuBoff/King 2000 Leonard D. Duboff / Christy O. King, *Art Law in a Nutshell;* West Group, St. Paul, 2000, p. 49.

[51] Adam/Burns 2011.

normally not allowed to bid), but a kind of a part owner.[52] The current trend goes in the direction of forbidding guarantors from bidding during the auction in order to limit conflict of interest and to increase transparency. However, I could not prove this development any further.

2.5 Legal Settings

2.5.1 General

The guarantee represents an assurance by one party to stand for the correct fulfilment of the obligation of another party. In other words, a guarantee is a promise by one person to answer for the due performance of the obligation of another person.[53] The legal description of the guarantee stipulates: "A guarantee is a contractual obligation undertaken by one person (described variously as the "guarantor", "surety", or "obligor") in which he or she promises that (a) a second person (known in the law of guarantee as the "principal", but often referred to as the "debtor", or "borrower" in guarantee contracts) shall perform a contract or fulfil some other obligation, but (b) that if the principal does not, the surety will do so in the place of the principal".[54]
Any obligation, which is possible in the legal framework, falls under the guaranteed obligation. In most cases the guarantee contract is a kind of security contract, which is commonly used to secure commercial transactions.[55]

In this essay, I limit myself to guarantees in the auction market, namely the auction house guarantees and third party guarantees, which are used by auction houses directly in connection with auction sales.
If we take the aforementioned description of the guarantee and put it into the art market situation, that is in the auction house guarantee situation, we can observe a difference in the role of the principal. As the nature of auction

[52] Graddy/Hamilton Kathryn Graddy and Jonathan Hamilton, *Auction House Guarantees for Works of Art,* on 16 May 2014, Working Paper Series, Brandeis University and University of Florida / Economics Department, p. 2.
[53] McGuinness 2013 Kevin McGuinness, *„The Law of Guarantee"*; LexisNexis Canada, 2013, p. 1.
[54] Ibid, p. 7.
[55] Ibid, p. 1.

houses lies in the fact that they hardly ever sell all the lots, the guarantee goes much further as the seller receives a guarantee for a future scenario, which may or may not occur. This future auction sale does not have an obligation yet, or a contract. Lots are offered to the public in an auction, but the end-buyer, who is the principal according to above definition, is not obliged to buy in advance. So, the auction houses' guarantee clauses are of a very specific nature. Several legal constructs are possible and will be discussed further below.

In the case of the auction house guarantee, the auction house plays the role of the guarantor, who will pay the price and buy the artwork in case no other buyer is found.
In the case of the third party guarantee the role of the auction house and the risk will be moved to a third party who promises the auction house that it will buy an artwork for a minimum stipulated price at the auction in the event of an absent bid from any other buyer. Now, the guarantor is a third party.
In both cases the seller has the security that the artwork will find a new buyer and that s/he will at least get the fixed "guaranteed" price.

2.5.2 Contractual Situation under Swiss Law

A. The Relationship between the Consignor and the Auctioneer

The laws regarding art auctions are very country specific and therefore I will limit myself to the legal situation under Swiss Private Law.
It is especially important to analyse the contractual relationship between the seller and the auctioneer. It is important to mention that few publications are available on the topic of auction house guarantees under Swiss Law. There is neither jurisdiction nor other strict regulations, which leaves a certain freedom and room for interpretation for such agreements.[56] Consequently, contractual freedom currently allows almost all kinds of various contractual

[56] Marchand 2014 Sylvain Marchand in Etudes en droit de l'art, Ed. Pierre Gabus et Anne Laure Bandle, *L'art a-t-il un prix? The Art of Pricing the Priceless*; Schulthess, Geneva, 2014, p. 16.

constructs.[57] There is no fixed form for a guarantee arrangement, and each contract has to be conducted on a case-by-case basis.[58]

There are several ways to see the contractual relation between the consignor and the auctioneer. The first is when the auctioneer acts in his/her own name and on his/her own account, which makes him/her the seller of the object (Art. 184 CO[59], Art. 32 CO); the second type is when the auctioneer acts in his/her own name, but not on his/her own account (Art. 425 CO); the last one is the auctioneer's role as agent – acting in the name and on account of a third party (Art. 412 CO).[60]

Normally, and according to Swiss Law, the contract between the seller and the auction house is that of the commission according to Art. 425 II CO, which refers to Art. 394 I CO, where defines the provisions of the mandate. By accepting an order according to Art. 394 I CO the commissioner is obliged to perform the transmitted businesses and services accordingly.

The promise to buy the artwork at the guaranteed price represents an extra agreement and therefore an additional contractual relation arises between the auctioneer and the seller.[61] That is, the sale and purchase agreement between the seller and the auction house.[62] Art. 184 I CO says that the sales agreement obliges the seller to give the sales object and property rights to the buyer, while the buyer has to pay the price. The auction house is obliged to perform its best in order to sell the artwork for the highest price possible, which is not easy due to the uncertainty of the auction business. The auction house is not interested in buying the artwork, rather its goal is to obtain the highest premium possible. Therefore, it will do all that it can to sell the lot and

[57] Ibid, p. 28.
[58] Feldman/Weil 1986, p. 92.
[59] CO stands for Swiss Code of Obligations, Bundesgesetz betreffend die Ergänzung des Schweizerischen Zivilgesetzbuches (Fünfter Teil: Obligationenrecht), from 30 March 1911 (status as of 1 July 2014).
[60] Glaus 2004 Dr. Bruno Glaus, *Die Haftung des Auktionators für Sachmängel gegenüber dem Ersteigerer (in 2.1 Verschiedene Handlungsweisen des Versteigerers)* in Jusletter, on 15 June 2004, http://www.glaus.com/bilderpdf/2wirtschaftsrecht/haftung_aukt.html, last access on 27.02.2015.
[61] Becker 2011 Joelle Becker, *La vente aus enchères d'objets d'art en droit privé suisse: représentation, relations contractuelles et responsabilité*; Schulthess, Geneva, 2001, p. 58.
[62] Ibid.

to sell it for the highest price possible. At the end of the auction sale the auction house is obliged to deliver a success to the seller and will have to execute the contract itself if it does not sell the guaranteed lot to a third buyer.[63]

The auction house is also liable for success in the case that the amount of the sale is higher than the guaranteed price, but insufficient to allow the auction house to collect its fees without affecting the guaranteed price. This situation is the same as if the lot had failed to sell at the guaranteed price.[64] The auction will then acquire the lot itself and pay the guaranteed minimum price.

However, the sale purchase agreement in the aforementioned constellation is a conditional contract as it only takes place in the case that no other party buys the lot at the auction. This condition depends on an uncertain event, which determines whether the contract of purchase has to be executed between the auctioneer and the seller of the lot.[65] Art. 151 CO describes the suspensory condition of the purchase contract: a conditioned contract is a contract whose binding character is dependent on the entry of an uncertain fact.

In case the condition is met, the contract has to be executed. The auctioneer has to pay the arranged price to the seller and the seller has to transfer the property of the lot to the auction house. Consequently, the auction house makes a binding offer to the seller until the end of the auction sale. Special arrangements can be included in the contract, such as the consent of the seller to the sale of the lot.[66] If the item fails to sell at auction the possibility remains open to the client to decline the guaranteed price if s/he would prefer to get the object back.[67]

Contrary to the opinion of Professor Marchand, who argues that the unsold lot should be removed from the auction sale[68] and then acquired by the auction house, I hold the opinion that the whole construct of the guarantee

[63] Ibid.
[64] Marchand 2014, p. 21.
[65] Becker 2011, p. 58.
[66] Ibid.
[67] Marchand 2014, p. 25.
[68] Marchand 2014, p. 22.

does not make sense if the guaranteed lot has to be removed. Moreover, the buyer and other involved parties would likely be interested in seeing the price reflected in the database (let us assume that the guaranteed price will be mostly seen as worth including in the database of sales).
The auction sale for the guaranteed object has to take place as per the agreed procedure in the case that the lot was not bought or sells for less. The lot should be sold within the auction sale frame so that it does not become a bought-in. The auction house cannot always envisage the result of the auction sale, both whether it will be sold and at which price. It is important for all parties involved that this lot does not become a “bought-in” as it has then failed at the auction and will have the reputation of being an unsold object for several years. In the case that the lot does not sell or sells for less than the guaranteed price, the guaranteed sum at which the guarantor acquired the lot will be reflected in the database (for example, Artprice.com).
The same opinion was found in the publication by Don Thompson, who states that an artwork with a guarantee can never become a bought-in.[69] Interestingly, at the last Contemporary November Evening Sale in New York, two guaranteed lots at Sotheby’s were not sold and are also registered as not sold in Artprice database.

The terms and conditions of auction houses normally do not contain any details regarding the contractual part of the guarantees, as they have to be discussed and settled on a case-by-case basis, bearing in mind the amount and the conditions of the sale.

Due to the fact that there is no strict regulation or jurisdiction on auction guarantee clauses under Swiss law, there are several interpretations of such contracts.
In contrast to the above-described type of conditional sale, Sylvain Marchand tends to see auction guarantees as unilateral promises to purchase[70] rather than as conditional sales. The distinction between two different types of obligations is important in regards to the transfer of property and within the object’s property its risks. If we have a conditional sale agreement, the

[69] Thompson 2014, p.161.
[70] Marchand 2014, p. 23.

ownership of the object passes to the auction house at the moment the condition is fulfilled, which means when the object fails to be sold at the auction.

In the case that we consider the agreement as a promise by the auction house to purchase (but no obligation to sell by the seller), the sale only takes place when the seller declares that s/he intends to transfer ownership of the object upon receiving the guaranteed price.[71]

B. The Relationship Involving the Third Party Guarantor

The above section was devoted to the description of the relationship between the auction house and the seller.

In the case of the third party guarantee, we have one more party involved, which is the third party investor. However, the applicable contract relevant to the seller is that of the auction house and seller even in case of the third party guarantee. This is the guarantee contract. Such a guarantee contract can, in theory, govern various topics, such as the right of the consignor's cooperation in regards to the third party guarantor, the conditions of the guarantee and the scenario in the event of non-performance from the guarantor's side.[72] Furthermore, the contract could also contain information on what would happen in case the artwork falls under any restitution clause or appears as being a fake.[73] On the other side, it could also govern what happens in case the auction sale fails at the fault of the consignor.[74] Sometimes the seller does not know whether there is a third party investor behind the auction house or not. And even if the seller knows that there might be a third party involved, the third party investor remains anonymous. Therefore, the above description (A.) would apply as for the seller. Normally, there is no contract between the seller and the third party guarantor.

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[71] Marchand 2014, p. 23.
[72] Mercker/Mues 2010 Florian Mercker and Gabor Mues, *Was bedeutet denn unwiderruflich?,* in Frankfurter Allgemeine Zeitung, 24 May 2010, http://www.faz.net/-gyz-y6km, last access on 08.04.2015.
[73] Ibid.
[74] Ibid.

The auction house will then arrange another contract in case of the third party coverage, directly with the third party investor.[75] This contract is the financing agreement and is highly confidential. Consequently I could not find an example of such a contract in the course of writing this paper.

The usual practice of the auction houses is to give a guarantee to the consignor and then to re-sell the guarantee to a third party investor.[76] However, in most cases, auction houses will not give a guarantee to a consignor before having a possible dealer or collector in mind or possibly even before pre-discussing with a third party.

[75] see Christies website: http://www.christies.com/lotfinder/paintings/gerhard-richter-demo-5846093-details.aspx?pos=38&intObjectID=5846093&sid=; http://www.christies.com/lotfinder/paintings/georg-baselitz-der-bruckechor-5846057-details.aspx?pos=1&intObjectID=5846057&sid= „...cases where Christie's holds the financial interest on its own, and in cases where Christie's has financed all or a part of such interest through a third party." „Christie's may choose to assume this financial risk on its own or may contract with a third party for such third party to assume all or part of this financial risk.", last access on 3.4.2015.

[76] Edelman 2014 Asher Edelman, *The Strangely Attractive Case of Guaranteed Lots at Auction* in Artnet, on 11 May 2014, https://news.artnet.com/market/the-strangely-attractive-case-of-guaranteed-lots-at-auction-15047, last access on 1.4.2015.

3 The Guarantor

3.1 Auction House Side

3.1.1 Business Acquisition

Auction houses use guarantees to help ensure permanent supply of high quality lots[77], which are fresh to the market and on demand. It is the task of the auction house to find interesting artworks on an on-going basis and it is not always easy to convince a collector to sell a masterpiece unless there is a secured reward for the selling party. Therefore, guarantees are instruments that the auction houses use in the acquisition process to secure business.[78]
At Christie's auction sale of Post-War and Contemporary artworks in New York in May 2014, at least 39 from 72 lots were guaranteed.[79]
It is in the interest of the auction house to have as many lots backed with a third party guarantee because in this way they have a high rate of sales virtually assured.

3.1.2 Increasing Profitability?

Are guarantees helping the auction houses to increase their profitability? Or are auction houses loosing money because of guarantees? According to Sotheby's CEO William Ruprecht, the number of guarantees in 2014 increased and they were "meaningfully profitable to the company." [80] According to an article in *The New York Times* from March 2015, sellers have the winning position, benefiting even more from the guarantees than the

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[77] Schack 2009 Haimo Schack, *Kunst und Recht*; Mohr Siebeck, Tübingen, 2009, p. 66.
[78] Bowley 2015.
[79] Tully 2014 Kathryn Tully, *In May's Blockbuster Art Sales, Auction Houses Will Guarantee More High Prices* in Forbes, on 5 May 2014, http://www.forbes.com/sites/kathryntully/2014/05/05/in-mays-blockbuster-art-sales-auction-houses-will-guarantee-more-high-prices/, last access on 27.02.2015.
[80] Rosenbaum 2014 Lee Rosenbaum, "*Meaningfully Profitable": Sotheby's Bill Ruprecht on the Performance of Auction Guarantees*, in Artsjournal, on 10 November 2014, http://www.artsjournal.com/culturegrrl/2014/11/meaningfully-profitable-sothebys-bill-ruprecht-on-the-performance-of-auction-guarantees.html, last access on 19.02.2015.

auction houses.[81] As auction margins are currently very thin, auction houses are searching for new opportunities to increase profitability.

Third party guarantees are interesting for an auction house as they do not pose a risk to the house and in case the artwork achieves a higher price than the reserve, the extra money will be split between the auction house and the third party guarantor after the agreed amount of the upside has been assigned to the consignor. "Sotheby's may reduce its financial exposure under auction guarantees through contractual risk and reward sharing arrangements under which a counterparty commits to bid a predetermined price on the guaranteed property."[82]

As third party guarantees are often issued for more valuable objects, they represent an interesting instrument for the auction houses to increase their profit. The situation could be even more profitable for the auction house than when it is the guarantor itself ("…auction commission margins and Sotheby's share of any auction guarantee overage could potentially improve, as the buyer's premium and any overage would not be shared with an irrevocable bid counterparty…"[83]), but the risk involved in such deals will keep it from being used in too many cases ("but Sotheby's could also be exposed to auction guarantee losses and/or deterioration in auction commission margins if the underlying property fails to sell at the minimum guaranteed price"[84]).

The reason for thin margins is that the auction house gives a part of its commission, which is how they originally earn money, to the seller and/or to the third party guarantor in order to try to get the best works on consignment and remain competitive.[85] The reduction in the commission must be filled with new money, such as from the guarantees. But even guarantees themselves when issued by the auction house are very risky for the profit of the auction house. Not only do the commissions lead auction houses to thin

[81] Reyburn 2015, Scott Reyburn, *At Auctions, Who Benefits Most From Art-Market Boom?,* in The New York Times, on 6 March 2015, http://www.nytimes.com/2015/03/09/arts/international/at-auctions-who-benefits-most-from-art-market-boom.html?_r=0, last access on 22.03.2015.

[82] Sotheby' Annual Report 2013, p. 93, Note 18.

[83] Ibid.

[84] Ibid.

[85] Bowley 2015.

margins, but also the fact that auction houses provide loans to their clients, as well as flexible payment schedules.[86]

The costs around the blockbuster auction sales are immense. Guarantees and all the costs around guarantees are enormous as the auction house needs to cover all the insurance, transportation and cataloguing costs, not to mention the costs of monograph catalogues, touring exhibitions, private events, cocktail parties and other publicity costs.[87]
The costs are also increasing due to the competition battle between Christie's and Sotheby's. One example is the sale of the estate of Mrs Sidney Brody.[88] In this case the consignor was approached with a proposed catalogue in several variations. One of the auction houses also proposed to fly the art pieces to six important cities to show them to top collectors; another proposal was to imitate the atmosphere of the Brody California home in the auction room.[89]
Auction houses must make decisions about how much money to spend trying to attract the public, buyers and collectors, as by reducing these costs they may be able to increase their profitability.

3.1.3 Guarantees as a Marketing Tool

Apart from the use of the guarantee as a tool to attract business, it also serves as a marketing tool. As guarantees are reserved for very special top-class artworks, the high valued pieces of art are also meant to attract and generate buzz. The marketing effect of the guaranteed object is big. In many cases the artworks that appear in the press and/or that tour around the world in various previews and exhibitions are guaranteed objects. The idea behind the marketing campaign is to attract the public, and finally to attract future business buyers as well as sellers of artworks. So, marketing serves the business strategy of reaching out for new business, for new buyers, etc.

The blockbuster auction sales are intrinsically marketing effects in addition to

[86] Horowitz 2011, p. 194.
[87] Mason 2004, p. 129.
[88] Thompson 2014, p.126.
[89] Thompson 2014, p.127.

all other effects, which such a sale has. When the public sees and reads the name of the prominent collectors or a particular collection, their memory will be connected with the specific auction house.

Consequently, such blockbuster sales and the sale of guaranteed objects within them have the potential to create hype both in and outside of the art world. The view of the public will then not correspond to the situation in reality. Art market professionals know how much occurs besides such blockbuster sales, and that in reality the deals have been pre-discussed and even made before the auction takes place. The auction itself serves to make the pre-arranged and settled results public. However, the public often only reads and hears about the record prices, such as *Andy Warhol's Painting of Elvis Presley Fetches GBP 82 Million at Auction*[90] or *Epic Christie's USD 852.9 Million Blockbuster Contemporary Art Sale Is the Highest Ever*[91]. The media reports have, as usual, a very important component in the whole marketing campaign.

However, it is important to remember that the top art market that we see and hear about is not the whole art market. In reality most of the art objects are sold in the small to mid-size art market with prices different to the guaranteed ones. The fact that the reality is not only about the great sales happening at auction can create a sham situation. The art market could be somehow exploited and simulated through these marketing effects.

3.1.4 Auction House as the Guarantor

The guarantee contract stipulates the relationship between the auction house and the seller on the agreement of guaranteeing a minimum price for a specific artwork or a part of it or even the whole group of lots.[92] Irrespective

[90] Rahman 2014 Abdi Rahman*, Andy Warhol's Painting of Elvis Presley Fetches £82 Million at Auction,* in The Hollywood Reporter, on 12 November 2014, http://www.hollywoodreporter.com/news/andy-warhols-painting-elvis-presley-748729, last access on 8.3.2015.
[91] Kinsella 2014 Eileen Kinsella, *Epic Christie's $852.9 Million Blockbuster Contemporary Art Sale Is the Highest Ever*, in ArtNet News, on 12 November 2014, http://news.artnet.com/art-world/epic-christies-8529-million-blockbuster-contemporary-art-sale-is-the-highest-ever-166404/, last access on 8.3.2015.
[92] Lerner/Bresler 2012, p. 318.

of the final auction outcome, the auction house will be obliged to pay the minimum guaranteed price to the seller. Furthermore, the auction house is not free to decide whether or not to put the guaranteed lot into the auction.[93] As soon as the contract is signed, it is the auction house's obligation to include the artwork in the auction sale. In comparison to third parties, the auction house is not allowed to bid in the auction in case it has guaranteed an artwork or a series of artworks itself.
If the lot remains unsold, the auction house will acquire ownership of that lot. It can then re-sell it in a future sale. At Sotheby's, until the object is sold, it is recorded as inventory on the consolidated balance sheets.[94] In case the lot is sold for a higher price than the agreed guaranteed price, the upside will be divided between the auction house and the seller as per the guarantee contract regardless of the buyer's premium, which the auction house gets as usual.
When an auction house makes a guarantee it could be entitled to receive a higher seller commission.[95] "As a general rule, the closer the guarantee comes to the low estimate, the greater the auction house's cut of the hammer price beyond the low estimate is. If a consignor is guaranteed, say, 75% of the low estimate, the auction house may receive 25% of the hammer price exceeding the low estimate; if a consignor is guaranteed 85% of the low estimate, the auction house may receive 35% of the hammer price exceeding the low estimate."[96]

Sotheby's informs the public which works are guaranteed at the end of the auction catalogue in the "Buying at Auction" section under the "Guaranteed Property" heading: "The seller of lots with this symbol (°) has been guaranteed a minimum price from one or a series of auctions. This guarantee may be provided by Sotheby's, by a third party or jointly by Sotheby's and a

[93] Becker 2011, p. 44.
[94] Sotheby' Annual Report 2013, p. 93, Note 18.
[95] Becker 2011, p. 44.
[96] Lerner/Bresler 2012, p. 318.

third party."[97] Sotheby's could have USD 300 million on net outstanding guarantees.[98]

Christie's informs the buyers in a similar way of possible guaranteed lots: "On occasion, Christie's has a direct financial interest in lots consigned for sale, which may include guaranteeing a minimum price or making an advance to the consignor that is secured solely by consigned property. Such property is identified in the catalogue with the symbol º next to the lot number. This symbol will be used both in cases where Christie's holds the financial interest on its own, and in cases where Christie's has financed all or part of such interest through third parties".[99]

Taking a closer look at the auction catalogues and as per the description of the lots inside, we can see that it is not always possible to know who is behind the guarantee – the auction house, the third party or even both.

3.1.5 Risks

The most important risk for the auction house is that the guaranteed artwork does not sell. In this case the auction house has to pay the consignor. It will then have to find a buyer and sell it in a private sale or at a future auction; otherwise it will suffer a financial loss.[100] So, the auction house remains "sitting" on the bought artworks, waiting to sell them at the next possible opportunity.

Removing risks from sellers, which can be reasonable in the case of museums as seller or similar situations, the risk has been moved to the auction house. This problem reached its peak during the crisis of 2008 and

[97] Sotheby's website, „*Buying at Auction*", http://www.sothebys.com/content/dam/sothebys/PDFs/cob/T00141-COS.pdf, last access on 23.02.2015.

[98] Sotheby' Annual Report 2013, p. 93, Note 18.

[99] Christie's website, *„Buying at Christie's",* https://www.christies.com/LotFinder/AbsenteeBidding/ImportantInfo.aspx?saleid=22142, last access on 23.02.2015.

[100] Reeves/Boll 1991 Van Kirk Reeves / Jan M. Boll, *General Report, Auction Sales and Conditions,* in Martine Briat / Judith A. Freedberg (Ed.), *La Vente internationale d'oeuvres d'art: le commerce international de l'art et le droit*; Paris (ICC), Deventer (Kluwer), 1991, p. 359.

led to the auction houses making strategic changes and shifting the risk to third parties.[101]

Another problem with guarantees is the issue of neutrality. The public expects to receive neutral advice from an auction house, which also lays in the nature of the auction house itself. Actions involving guarantees were very much discussed and criticized due to the fact that "auctioneers are supposed to give unbiased and equal advice to buyers as well as sellers…"[102] However, already in 1990, in an interview to *The New York Times*, Christopher Davidge[103] mentioned that it is feasible to both give guarantees as well as maintain professional standards, which are expected by the clients.[104] Another aspect of the neutrality issue is that of the third party guarantor's right to bid on the guaranteed objects. However, it would be difficult otherwise to guarantee the best price of the object to the seller.[105]

The transparency issue within the general discussion and trend in the direction of the regulation of the international art market is also existent in the guarantees system.[106] Traditionally, the role of the auctioneer is an independent one, serving "as the impartial arbitrator between buyer and seller with no other interest than his service fee."[107] It seems that her/his role is also currently in transition. It is also questionable how much regulation and transparency is needed in the art market and wished for by the involved players. According to the dealers, the auction system is one of the fields in the art market that really requires regulation.[108]

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[101] Tully 2011 Judd Tully, *Assurance Policies: Third-Party Guarantees May Reduce Risk and Yield Rewards* in Blouinartinfo (*"Assurance Policies" originally appeared in the September 2011 issue of* Art+Auction) on 22 September 2011, http://www.blouinartinfo.com/news/story/749117/assurance-policies-third-party-guarantees-may-reduce-risk-and, last access on 18.02.2015.
[102] Goodwin 2008 James Goodwin, *The International Art Markets. The essential guide for collectors and investors*; Kogan Page Limited, London, 2008, p. 8.
[103] Christopher Davidge was CEO of Christie's in 1993-1996.
[104] Mason 2004, p. 84-85.
[105] Pogrebin/Flynn 2013, Robin Pogrebin and Kevin Flynn, *As Art Values Rise, So Do Concerns About Market's Oversight* in The New York Times, on 27 January 2013, http://www.nytimes.com/2013/01/28/arts/design/as-art-market-rise-so-do-questions-of-oversight.html?pagewanted=all&_r=0, last access on 27.02.2015.
[106] Adam/Burns 2011.
[107] Reeves/Boll 1991, p. 359.
[108] Pogrebin/Flynn 2013.

Another practice, which is also relevant in connection with auction guarantees, is chandelier bidding[109], also called consecutive bidding. Chandelier bids are defined as non-existent bids and derive their name from the fact that the auctioneer is looking at something undefined in the room, calling out such bids. Direct connection with the guarantees system can appear when the auctioneer is calling out non-existent bids to prompt the public in the auction room to come closer to the reserve price, which has been mostly agreed on in advance to be guaranteed by the auction house or a third party.[110] The problem is that present bidders do not know that there is an undisclosed reserve behind the bids that is trying to be reached with chandelier bids. People then think it is a real bidder involved and will be encouraged to bid not having the transparent view of what is behind such bids.

New York City has tried to forbid this practice, issuing ten various bills since 1991, which have led to several amendments, but not the prohibition itself.[111] Yet, some argue that it is difficult and important to create a special atmosphere in the auction room and chandelier bids are needed for this momentum.[112]

Furthermore, the fact that auction houses provide guarantees also shows some problem inside the art market in relation to the primary market, as "guarantees successfully divert some artwork from galleries to the auction market."[113] Actually, there is a significant conflict of interest as the art market is in movement[114], shifting the traditional tasks from one player to another, such as auction houses opening galleries, organizing exhibitions as well as selling to collectors in private sales. In most cases this refers to the contemporary art sales, which were originally controlled by the galleries.

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[109] Another definition for the chandelier bidding is that of „Phantom Bids" in: DuBoff/King 2000, p. 49.

[110] Grant 2007 Daniel Grant, *Legislators Seek To Stop „Chandelier Bidding" At Auction* in ArtNews, on 4 September 2007, http://www.artnews.com/2007/09/04/legislators-seek-to-stop-chandelier-bidding-at-auction/, last access on 6.3.2015.

[111] Vadi/Schneider 2014 Ed. by Valentina Vadi / Hildegard E. G. S., *Art, Cultural Heritage and the Market: Ethical and Legal Issues*; Springer, Berlin-Heidelberg, 2014, p. 335.

[112] Grant 2007.

[113] Lerner/Bresler 2012, p. 319.

[114] Dalley 2014 Jan Dalley, *Winners and Loosers from the Art Market New Rules,* in The Financial Times, on 27 June 2014, http://www.ft.com/intl/cms/s/0/55ba02ec-fc51-11e3-98b8-00144feab7de.html, last access on 27.02.2015.

3.2 Third Party as a Guarantor

3.2.1 Instrument for Super Rich Individuals

Third party guarantors have a contract with the auction house, which obliges them to “guarantee” a certain amount on a specific work of art. These third party guarantors are also called irrevocable bidders as they promise to place a bid, which cannot be cancelled.[115] The third party guarantee can refer to a share of a lot[116], the whole lot or a group of lots. Depending on each and every contract, the auction house can be obliged by the consignor to advance (cash in advance) the whole guaranteed amount or a portion of it prior the auction sale.[117]

Since 2008 Sotheby’s has informed the public of a third party guarantee placing a horseshoe ( ), which means an irrevocable bid, next to the artwork’s name. Christie’s followed in 2010 with the communication of a possible third party guarantee in a separate text. Taking a look at online auction catalogues today we can see similar explanations by both auction houses.

Christie’s, in its online catalogue, informs the public with the Special Notice of a possible guarantee. Reading the text and interpreting it one can sometimes be sure that there is a third party guarantee (“Christie’s guarantee of a minimum price for this lot has been fully financed through third parties“[118]). But in the most cases we do not know whether it is an auction guarantee or a split one or even maybe a third party guarantee. Introduce the quote - “On occasion, Christie's has a direct financial interest in lots consigned for sale which may include guaranteeing a minimum price or making an advance to the consignor that is secured solely by consigned property. This is such a lot. This indicates both in cases where Christie's holds the financial interest on its own, and in cases where Christie's has financed all or a part of such interest through a third party. Such third parties generally benefit financially if a

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[115] Rozell 2014, p 171.

[116] Sotheby’s website, *Guaranteed Property*, http://www.sothebys.com/content/dam/sothebys/PDFs/cob/T00141-COS.pdf, last access on 24.02.2015.

[117] Sotheby’s Annual Report 2013, p. 93, Note 18.

[118] Christie’s website, http://www.christies.com/lotfinder/paintings/christopher-wool-untitled-5846094-details.aspx?pos=37&intObjectID=5846094&sid=, last access on 06.04.2015.

guaranteed lot is sold successfully and may incur a loss if the sale is not successful".[119]

Sotheby's has a more visual explanation of the third party guarantee putting the horseshoe-sign next to the °-sign. When we see these two signs together it means that there is a third party involved, but we do not know whether it is only a third party or whether it could also be in part guaranteed by the auction house itself. It would be much clearer and more efficient if only one sign was shown, meaning either third party guarantee () or the auction guarantee (°). Furthermore, Sotheby's gives notice that "If the irrevocable bid is not secured until after the printing of the auction catalogue, a pre-lot announcement will be made indicating that there is an irrevocable bid on the lot".[120]

In comparison to US law, which is now applied to all affiliates of Christie's and Sotheby's, and requires the house to mark the artworks in the catalogue that are guaranteed, German law does not contain such a regulation. In Germany, auction houses would be allowed to include guaranteed artworks in an auction sale without marking them as such in the catalogue.[121]

"The first guarantee funded by a third party is believed to date back to November 1999, when Sotheby's found a backer to pledge USD 40 million for Pablo Picasso's *Seated Woman in a Garden*, which had been consigned by Eleanore Saidenberg, Picasso's long-time American dealer, and her husband, Daniel".[122]

The following scenario will take place depending on whether the piece of art will be sold or not and at what price. In the case that the object to be sold is sold for a higher price than the guarantee, the guarantor will get a share of the sum, which is higher than the guaranteed amount. In case the artwork remains unsold, the guarantor gets the artwork.[123] At Sotheby's, "third parties providing all or part of a guarantee, benefit financially if a guaranteed lot is

[119] Christie's website, http://www.christies.com/lotfinder/paintings/gerhard-richter-demo-5846093-details.aspx?pos=38&intObjectID=5846093&sid=, last access on 06.04.2015.
[120] Sotheby's website, http://www.sothebys.com/en/auctions/ecatalogue/2014/contemporary-art-evening-sale-n09221/lot.40.html, last access on 26.04. 2015.
[121] Mercker/Mues 2010.
[122] The Economist, *Financial machinations at auctions,* in The Economist, on 18 November 2011, http://www.economist.com/blogs/prospero/2011/11/art-market, last access on 20.02.2015.
[123] Rozell 2014, p. 171.

sold successfully and may incur a loss if the sale is not successful."[124] Christie's has a similar regulation: "When a third party agrees to finance all or part of Christie's interest in a lot, it takes on all or part of the risk of the lot not being sold, and will be remunerated in exchange for accepting this risk. The third party may also bid for the lot. Where it does so, and is the successful bidder, the remuneration may be netted against the final purchase price. If the lot is not sold, the third party may incur a loss."[125]

"The third party guarantee is an arrangement whereby a third party (generally a cash-rich art dealer or a major art collector) would either share with the house or fully bankroll the risk of the amount of the guarantee when a work is offered for sale by the auction house. If the work is sold successfully, the third party obtains a financial benefit, that is, a share of the buyer's premium and a share of the upside over the guarantee price. If the work is not sold, the third party must buy the work at the guarantee price plus pay 100% of the buyer's premium."[126]

Third party guarantors remain anonymous and each time such a guarantee deal takes place all the details will be discussed separately and negotiated case by case.[127] Even for the seller the third party remains unknown in most cases.[128]

Third party guarantees are an opportunity for wealthy collectors and art dealers to play on the art market without loosing.[129] Dealers such as Bill Acquavella, David Nahmad, Adam Lindemann and collectors such as Steve Cohen, Pierre Chen and members of the Qatari royal family are known for their involvement in third party guarantees.[130]

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[124] Sotheby's website, *„Buying at Auction"*, http://www.sothebys.com/content/dam/sothebys/PDFs/cob/T00141-COS.pdf, last access on 23.02.2015.

[125] Christie's website, *„Buying at Christie's",* https://www.christies.com/LotFinder/AbsenteeBidding/ImportantInfo.aspx?saleid=22142, last access on 23.02.2015.

[126] Lerner/Bresler 2012, p. 321.

[127] Tully 2011.

[128] see controversial opinion as of the guarantor's anonymity in Graddy/Hamilton 2014, p. 8.

[129] Adam/Burnes 2011.

[130] The Economist, *Financial machinations at auctions* in The Economist, on 18 November 2011, http://www.economist.com/blogs/prospero/2011/11/art-market, last access on 20.02.2015.

3.2.2 The Beneficial Position

A third party guarantor agrees to guarantee a certain artwork of an artist, which is interesting for him/her. It means that the guarantor actually wants to have the artwork.[131] With the instrument of the third party guarantee the collector or the dealer may even get it for a good price and s/he can even earn money in case the price grows and surpasses the discussed guaranteed amount.

For a wealthy collector this opportunity represents a winning position as s/he can at least have the desired artwork for a "moderate" price at the end of the auction. And in the best case, in addition to the artwork, the collector will also get money. According to an unnamed source, the third party guarantor can get from 50% up to 80% of the upside.[132] An "upside" is the difference between the guaranteed price and the price, which was achieved at the auction.[133]

Apart from the portion from the upside, the guarantor may enjoy other special treatment from the auction house, such as "profit shares, commission shares and financing fees"[134] to be discussed and negotiated in each and every case separately.

"One controversy revolves around the way third party guarantors earn "financing fees" at the two main houses. At Christie's guarantors earn a fee whether they end up buying the work or not; at Sotheby's the fee is only paid if the guarantor does not in the end acquire the artwork."[135] The explanation is that the guarantor shall not benefit twice. And this fact also shows that the guarantees system at Christie's is more interesting from the guarantor's perspective. However from the buyers' perspective, the model used at Sotheby's is fairer as the guarantor who is bidding and finally getting the

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[131] Adam/Burnes 2011.
[132] Tully 2011.
[133] *Sotheby's irrevocable bid explained*, 12.11.2008, http://artradarjournal.com/2008/11/12/sothebys-new-irrevocable-bid-explained-ft-saatchi/, last access on 19.02.2015.
[134] Sidorova 2014 Kira Sidorova, *Top Art Stories: Records and Guarantees* in galleryintell.com on 15 May 2014, http://www.galleryintell.com/post-war-contemporary-art-sales-new-york/, last access on 20.02.2015.
[135] The Economist, *Financial machinations at auctions* in The Economist, on 18 November 2011, http://www.economist.com/blogs/prospero/2011/11/art-market, last access on 20.02.2015 and Lerner/Bresler 2012, p. 322.

artwork above the guarantee amount does not get any monetary advantage (finance fee) from the house. Thus, the guarantor and bidders in the auction room are treated equally.[136]

Don Thompson gives an interesting example in his book on a New York based art dealer who possibly earned around USD 8.5 million giving guarantees for just three works, which sold for unexpectedly high prices.[137]

Another side of the beneficial position is the third party guarantor's opportunity to directly influence the market of a specific artist and maintain prices or even increase them. In many cases the third party guarantor will be interested in driving up the price as s/he can anyway only win – getting the artwork with rebate or getting more from the upside and eventually the commission.

Furthermore, involvement in the guarantees system brings the client closer to the auction house and strengthens their relationship. The collector or the dealer will get access to information, which might be interesting and of use for him/her and which is not available to other bidders.[138]

The third party guarantee is also very beneficial for the auction house as they can outsource the risk and shift it to the other party. Furthermore, they do not accumulate "burned" artworks in their storage, which also require proper maintenance including air-conditioning, insurance, etc.

3.2.3 Critics

The fact that the third party guarantor receives extra information and is not excluded from bidding at the auction is a delicate issue. Moreover, guarantors will actively use bidding in order to increase the price.[139] It is questionable whether such practices are ethical. Furthermore, it can represent a conflict of interest.

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[136] Graddy/Hamilton 2014, p. 9.

[137] Thompson 2014, Don Thompson, *The Supermodel and the Brillo Box*, New York, Palgrave Macmillian, 2014, p.161. These three works are: *Untitled* by Félix Gonzalez-Torres's sold at Phillips for USd 4.6 million, *Nude, Green Leaves and Bust* by Pablo Picasso sold at Christie's for USD 106.5 million and *Grande Tête Mince* by Alberto Giacometti sold for USD 54.3 million.

[138] The Economist, *Financial machinations at auctions* in The Economist, on 18 November 2011, http://www.economist.com/blogs/prospero/2011/11/art-market, last access on 20.02.2015.

[139] Rozell 2014, p. 171.

The overall situation on the global contemporary and modern art market and the current high prices and records at auctions is partly due to the guarantees. Critics argue that the guarantees are responsible for the current boom in the contemporary art market and question how long this situation can last. They ask whether the guarantee system is supporting the hype and the art bubble to increasingly grow.

The guarantor's beneficial position has a dangerous side. This is the possibility to manipulate the market. Both in guaranteeing and bidding there is a problematic position as by guaranteeing an artwork the third party ensures that it will not fail. Such bidding and heating the price is even more problematic as the third party tries to manipulate the price to make it as high as possible and still more favourable for herself/himself.

4 The Seller

Let's turn to the sellers' side and try to analyse what can motivate them to consign a work from their collection or stock.

First of all we have to define who the seller of an expensive artwork to be auctioned is. As of the nature of the third-guarantee business with high valued artworks and masterpieces, it must be a very rich collector or a mega art dealer.

What could be the reason behind signing such a guarantee contract? It can be difficult for passionate collectors to separate themselves from a nice artwork. They must have a really good reason for such third party participation. The mega dealer could be more interested in playing on the art market and to use such an option for investment purposes.

4.1 Art as an Investment

Art as an alternative investment not only has a financial aspect, but also an aesthetic one, which is very important. This is also the reason for different discussions and opinions about whether art can be seen as a pure investment ignoring its aesthetic aspect. This also explains why most art investors are also art lovers and art collectors. The idea of investment in art as pure investment might not be a good one and buying art should not only be seen as an investment. The art investor must also like and enjoy the artwork which makes the process of the investment a subjective one.

"If investment is your primary motive then it is better to avoid art and stick to more normal asset classes such as property, stocks and bonds. Art is a good investment but only for people who can afford to buy the right paintings and sell them at the right moment. In order to determine the right paintings and the right moment, one should have a lot of know-how and connections based on the art education or advice from art consultants. Art should be looked at primarily as a source of enjoyment and secondly as an excellent way of diversification and storing value for the future."[140]

Taking a look back in the history of art investment, we can observe that investments in art started to take place in the 1970s due to the huge growth in value of art objects. Since then two indexes have been established, which help to estimate value of the art. The first one is the Art Sales Index, founded in 1975 and which is based on fixed baskets in different categories with 30 to 40 artworks each. The values of these works are estimated by art market experts twice a year.[141]

The second one is the Mei Moses Fine Art Index, which is based on the long-term data of art purchases and sales. Jiangping Mei and Michael Moses, professors at the Stern School of Business at New York University, developed it. The idea is based on the original sale price of a specific precious painting, which is compared with the later re-selling price of the same artwork at Christie's or Sotheby's. The return is then calculated from the difference.[142]

Artprice is nowadays a very important database, which offers information on the global art market, including prices of artworks that were reached in different auctions. This data helps to decide, for example, whether you want to sell or buy an artwork, or invest in an artwork of a specific artist.

Even though we have several tools such as Art indexes and Artprice, art investment forecasting is more complicated compared to stock forecasting because there is no benchmark for the determination of art quality and its influence on the development of value of an artwork. However, it is possible to divide art investments into secure (Blue Chips) and insecure investment categories.[143] Secure artworks are artworks by artists, whose complete work (oeuvre) is already determined both in quantity and in quality.

In any case, investment in art should be considered as a long-term investment.

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[140] „Frequently asked questions on Russian art collecting, buying and selling", Agents / Dealers – An Authority on Russian art, web page, www.russianartdealer.com, last access on 29.04.2015.

[141] Boll 2009, p. 79.

[142] Wikipedia, web page, http://de.wikipedia.org/wiki/Mei_Moses_Fine_Art_Index, last access on 29.04.2015.

[143] Boll 2009, p. 80.

It is also important to bear in mind the costs, which arise in connection with an investment in art such as safety appliance, air conditioning, insurance costs, etc. An artwork should increase in value by 50% in 5 years in order to become profitable. In comparison to stocks, there is no return on art investments during possession of the work.[144]

4.2 Private Sale in the Context of an Auction

A sale based on a guarantee represents a kind of a private sale both for the seller and for the auction. There is not much left from the traditional auction sale in this kind of interaction. The auction house offers lots of attention, assistance and advice, interacting with high profile collectors or dealers and their exquisite artwork. Such a guaranteed sale represents a direct transaction at the forefront of the auction.

Sellers appreciate such a constellation as the price is fixed before the auction, and the auction itself could only have a positive effect. The price can only increase and exceed the guaranteed price. This represents a very optimistic situation for the seller.

The guarantee system works as a security for the seller. Furthermore, the seller does not have the risk that the artwork will become a bought-in.

As for the art market in general the seller, who is consigning high quality artworks, brings liquidity to the market.

4.3 Other Factors

What else besides investment and the securement of cash could motivate the seller to consign his/her work of art? Different reasons could play a role.

The collector might have new ideas about what s/he wants in his/her art collection. S/he may want to sell several pieces in order to get cash for new acquisitions. S/he may also wish to start a new collection, in a completely new direction and want to get rid of several artworks.

Moreover, it can also be the case that the client is currently encountering one of the three so-called D's: death, divorce or debt. In these conditions,

[144] Boll 2009, p. 81.

artworks are also sometimes to be sold. The guaranteed sale here is also a good and secure option.
Other factors could be social, such as social status or lifestyle ideas in the moving art market.

5 The Buyer

A potential buyer of an artwork likely attaches great importance to three factors, probably similar to any buyer of a valuable good.
First of all, the kind of artwork s/he intends to purchase needs to be available. This means that s/he needs access to the right sales channels or institutions and that the current owner of such work(s) is willing to sell them. This factor can be seen as a prerequisite for an art transaction. The auction house allows the buyer to get this access to an artwork.
The second factor is likely to be quality. A buyer will have certain expectations with regard to the quality of a good that s/he requires to be met. With regard to artworks, the provenance and exhibitions might be an important indicator of the quality.
Once a buyer has identified an artwork that is for sale and which also meets his/her demands in terms of quality criteria, s/he would usually try to purchase it at the lowest price possible.

On the one hand, one would assume that auction house guarantees should have a positive impact on the availability of artworks as well as on the quality of the artworks offered. Guarantees are an incentive or insurance for owners of artworks as they give them the comfort their work will be sold at a reasonable price. This helps auction houses to find sellers of high-quality artworks. However, guarantees might also lead to higher prices being paid for auctioned goods, which could be seen as a negative for the buyers. The higher price is explained through the fact that guaranteed artworks would be sold for more, as the guarantor (third party and/or auction) is interested in getting as high an overage as possible. The guarantor might bid in order to increase the price as s/he is in an advantageous position – either s/he will get the piece desired or a share of the overage. In both cases, and especially if the investor/collector really likes the artwork, s/he can only win. Furthermore, in the case that the guarantor is present in the auction room and is bidding (or participating via telephone), other buyers are in an unequal situation. The buyer, in contrast to the guarantor, does not know whether the guarantor is in the auction room and might be bidding against him/her.

These considerations show that auction house guarantees may have positive as well as negative effects for potential buyers. There seems to be a certain trade-off between these effects. However, it can be argued that even if guarantees lead to higher selling prices for top artworks, the works might not even be offered at an auction if the auction house were not to guarantee a certain hammer price. The above shows that the buyer’s position has several advantages in terms of top artworks and availability, but also a disadvantage in terms of price. The overall position of the buyer compared to the win-win position of the guarantor is less advantageous.

6 Guarantees and the Booming Contemporary Art Market

6.1 Contemporary Art Market: Rise and Hype

Talking about the art market, quite a lot of people today focus on contemporary art as this market plays a big role and has a prominent position in today's world. The importance of contemporary art has been increasingly growing in the last decades and especially since the mid 2000s.

The starting point was the Scull Auction Sale in 1973. This auction of artworks from the Scull Collection at Sotheby Parke Bernet on 18 October 1973 laid the ground for the development of contemporary sales at auctions.[145] The Sculls started to collect in the 1950s and belonged to the prominent American collectors of Minimal and Pop art. The sale of 50 artworks in 1973 was successful, collecting USD 2.2 million. After this sale both Christie's and Sotheby's started to hold contemporary art sales on a regular basis.[146] A new type of collector appeared as the demand for the contemporary art grew. The informative role of the auction house was immense and still remains very important. The auction houses publish auction results and, in this way, provide the public with valuable information.

Comparing the auction sales results we can observe that contemporary art definitely took over first place in the art market from Modern and Impressionist art in 2007.[147] After a short slowdown during the economic crisis the market has been continually building its strong position season by season. There are innumerable contemporary art fairs opening each year all over the world, important galleries are opening branches in various cities and more and more smaller galleries for contemporary art are opening. And, of course, the auction houses are taking an important position in the

[145] Hollein 1999 Max Hollein, *Zeitgenössische Kunst und der Kunstmarktboom*; Böhlau, Wien, 1999, p. 23.

[146] Ibid.

[147] Gleadell 2014 Colin Gleadell, *Why contemporary art keeps breaking records,* in The Telegraph, on 13 November 2014, http://www.telegraph.co.uk/culture/art/art-news/11229926/Christies-auction-record-what-it-means.html#disqus_thread, last access on 12.03.2015.

contemporary art market, offering artworks at sales. The contemporary art market has been internationalized and is very interactive.

Art market professionals as well as amateurs would like to participate in the contemporary art market as this market is currently generating very high prices. According to art market professionals the contemporary art market will realize auction prices in the USD billion ranges very soon.[148] In only fourteen years (2000-2014) the contemporary art market has grown by a factor of 10.[149] Thus, the idea of art as an investment would very much apply to contemporary art deals.

What are the reasons for such a rise and hype in the field of the contemporary art market? To understand and follow contemporary art trends, we can look at the reasons that have led to such a situation in the contemporary art market.

The fact that after 1973 auction houses started to hold contemporary art sales on a regular basis presented a possibility to a wider public to be aware and informed about contemporary art and its market.[150]
The rise of the contemporary market comes together with the overall economic growth and the increasing number of ultra high net worth individuals. This has consequently produced a rise of new collectors worldwide; particularly noticeable are the new collectors from the Middle East, Russia and China.
These collectors frequently like to show their money and in comparison to some well-established buyers, or in other words, old-school conservative collectors, they do not always remain anonymous when bidding at auctions. They use art partly as a social symbol or lifestyle tool. Moreover, in order to establish themselves, sometimes they even want people and the press to talk about them and make their new acquirements public. So, contemporary art becomes a part of the lifestyle, and they also establish it as a kind of fashion.

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[148] *Artprice: the Art Market heading towards billion-dollar auction pric*es, on 17 February 2015, http://finance.yahoo.com/news/artprice-art-market-heading-towards-120402650.html, last access on 12.03.2015.
[149] Ibid.
[150] Hollein 1999, p. 26.

Young, contemporary artists are ready to meet the demand coming from these new as well as established buyers, and thereby spurring this contemporary art fashion. There is also a new trend of experiencing and seeing art in the process of formation rather than only several years later in a retrospective exhibition.

The availability of contemporary artworks in galleries, art fairs and auctions worldwide makes it easily accessible to a wider collecting public. However, the huge demand and the high prices of artworks moves collecting to the high-end elite collectors.[151] As for the middle-size collectors, which are the core collector class, it is getting more and more difficult to obtain and afford these artworks.

A further development in the 21st century is the building of a huge number of new museums.[152]

Companies started to be interested in contemporary art and have built major corporate art collections worldwide.

One possible explanation for new buyers' interest in contemporary art could be the fact that contemporary art is not so complicated to understand and does not require a lot of art historical knowledge or a general art educational background.

The hype surrounding the contemporary art market is also seen in connection with the guarantees system. To secure highly appreciated contemporary works of art, auction houses propose straight or third party guarantees to consignors attracting both the seller to sell and the buyer to acquire great works, which are in demand. For a passionate art collector or dealer guarantees represent a great opportunity to buy an artwork or to invest and make a profit. Currently, the number and the volume of guaranteed artworks at contemporary auction sales are high. Looking back at the contemporary art evening sales of last November 2014 we can see that Christie's guaranteed USD 429.8 million and Sotheby's USD 184.2 million.[153]

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151 Gerlis 2014 Melanie Gerlis, *Art As An Investment? A Survey of Comparative Assets*; Lund Humphries, 2014, p. 165.

152 *Artprice: The Art Market heading towards billion-dollar auction pric*es, on 17 February 2015, http://finance.yahoo.com/news/artprice-art-market-heading-towards-120402650.html, last access on 12.03.2015.

153 Burns/ Pobric 2014 Charlotte Burns and Pac Pobric, *In auctions, unlike in life, there are guarantees,* in The Art Newspaper, on 14 November 2014, http://www.theartnewspaper.com/articles/In-auctions-unlike-in-life-there-are-

These numbers represent nearly half of the lots of that exact auction when compared to Christie's and Sotheby's overall selling results.[154]

So, the auction houses played and still play a crucial role in increasing the contemporary art market and also in increasing the general public and collectors' interest in contemporary artworks.

6.2 Dependency of Auction Houses on Contemporary Art Sales

Contemporary art is currently playing a major role in the art market, meaning that many art market players are dependent on the sales of contemporary artworks. In recent years auction houses have been acting more and more on the primary art market. Therefore, today auction houses also depend on the contemporary sales. As for contemporary auction sales there are two sales, which are especially important for both Christie's and Sotheby's. These sales are held in November and May in New York (Contemporary Evening Auction Sale).

As indicated above, the financial guarantees also play an important role in contemporary art sales. According to an article in *The Art Newspaper* the exact number of guaranteed artworks in the last contemporary evening sale was: 46% at Sotheby's on 11 November 2014 and 46% at Christie's on 12 November 2014.[155] For Christie's the result of the sale on 12 November 2014 represented a record as they sold artworks for USD 852.8 million in comparison to the previous sale in May 2014 of USD 745 million. Comparing Christie's November 2014 result to the Christie's result in May 2012 the growth in the value of contemporary sales lays at 120%.[156]

Analysing the Art Tactic Report for the year 2015 we can see that forecasters are optimistic about the development of the higher contemporary art market and predict that a USD 1 million plus segment in this market will continue to bring positive results.[157]

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guarantees/36281, last access on 12.3.2015; Counting together the guaranteed lots available online (final auction price including the buyer's premium), I came to a slightly different result, which is USD 521.7 million for Christie's and USD 185.8 million for Sotheby's during November 2014 Contemporary Evening Sale in New York.

[154] Burns/Pobric 2014.

[155] Ibid.

[156] Ibid.

[157] ArtTactic Outlook 2015, p.3.

We can assure ourselves of the importance of contemporary art sales in connection with guarantees by taking a look back to the Evening Contemporary Auction Sale last November in New York.
Christie's sold all of its 75 lots. From these 75 lots, 46 were sold between USD 1 million and USD 10 million. 42 lots were sold in a classical auction sale, i.e. without any guarantees, and 33 lots were guaranteed. We can see that 8 of the guaranteed lots were guaranteed through a third party. As for the remaining 25 lots, we do not know whether the auction house fully guaranteed them or shared the risk with a third party investor.
From the same 75 lots, 23 were sold for over USD 10 million, with 8 being sold directly and 15 involving a guarantee. 4 lots were fully backed by a third party guarantee and for the remaining 11 we do not know how the auction house structured the guarantee.
As for the direct third party guarantees we can see that in most cases the final price was set somewhere between the low and the high estimate.
Only 6 lots from the whole sale were sold below USD 1 million (three among them were guaranteed).
Total sales amount to USD 852.9 million including the buyer's premium.
Sotheby's Contemporary Evening Sale held in November 2014 in New York achieved the following numbers.
From a total of 67 lots, 46 sold for over USD 1 million. 26 of them sold directly and the remaining 20 lots involved a (third party) guarantee.

We can see that 12 of the 33 guaranteed lots were guaranteed through a third party. As for the remaining 21 lots, we do not know whether the auction house fully guaranteed them or shared the risk with a third party investor.
Of these 67 lots, 7 were sold for over USD 10 million. 2 were sold directly and 5 lots were sold through a guarantee. 14 lots sold below USD 1 million, while 8 lots were guaranteed. 10 lots from the sale remained unsold. Interestingly, two lots from the unsold lots were marked as guaranteed by the auction house (lot number 33 and 37). Lot 33 represents a monumental art object *Moon (Yellow)* by Jeff Koons, estimated to be worth between USD 12 to 18 million. Lot 37 is Andy Warhol's *Little Electric Chair*, estimated at USD 7.5 to 9.5 million. The auction house guaranteed both lots. Both negative

results are reflected in the database Artprice.com as “lot not sold”.
The overall sales amount for this sale at Sotheby’s was USD 343.7 million.

6.3 Analysis of Guarantees in Contemporary Auction Sales

In order to see the development of the guarantees in the frame of contemporary auction sales, I analyse the auction results from past years. For this analysis I took numbers from both Christie’s and Sotheby’s auction sales, concentrating on the November Contemporary Evening sale of both houses, which is annually held in New York. I split the results from 2008 to 2014 into the following groups: number of lots sold below USD 1 million and how many thereof were guaranteed; number of lots sold for USD 1-10 million and how many thereof were guaranteed, and number of lots sold for over USD 10 million and how many thereof were guaranteed. In addition, I also looked at total sales in USD million, total number of lots sold, total sales of guaranteed lots and how much thereof were sold above USD 10 million. Unsold and retrieved lots were not included in the analysis. Another important distinction is the number in brackets next to the guaranteed lots. This shows the number of confirmed third party guaranteed lots. However, this distinction is not always possible to make as we sometimes have both signs (at Sotheby’s: guaranteed property = ○, and irrevocable bid = ⋑) or there is not a final note next to the lot, which means there are financial interests held by the auction house and a third party. At Christie’s this would be “On occasion, Christie’s has a direct financial interest in lots consigned for sale which may include guaranteeing a minimum price or making an advance to the consignor that is secured solely by consigned party. This is such a lot. This indicates both cases in which Christie’s holds the financial interest on its own, and cases in which Christie’s has financed all or a part of such interest through a third party. Such third parties generally benefit financially if a guaranteed lot is sold successfully and may incur a loss if the sale is not successful.”[158] One of the reasons to look several years into the past is that

[158] Christie’s website, Example: http://www.christies.com/lotfinder/photographs/andreas-gursky-rhein-ii-5496716-details.aspx?from=salesummary&pos=14&intObjectID=5496716&sid=530750e5-2538-41b5-b0f7-ee8f7389fbfa, last access on 16.04 2015.

after the economic crisis of 2008 the auction houses started using guarantees again, concentrating more and more on third party guarantees.

Christie's	2008	2009	2010	2011	2012	2013	2014
Total Sales in USD millions	113.6	74.2	272.9	220.8	412.3	691.6	852.9
Total lots sold	44	39	70	55	67	64	75
... thereof guaranteed	21 * 47.7%	4 * 10.3%	6 (5) 8.6%	13 (9) 23.6%	25 (8) 37.3%	17 (9) 26.6%	33 (8) 44.0%
Lots sold below USD 1m	15	18	12	15	11	7	6
... thereof guaranteed	9 * 60.0%	0 * 0.0%	0 (0) 0.0%	2 (0) 13.3%	4 (0) 36.4%	1 (0) 14.3%	3 (0) 50.0%
Lots sold for USD 1m - 10m	27	20	55	36	45	41	46
... thereof guaranteed	11 * 40.7%	4 * 20.0%	4 (4) 7.3%	9 (8) 25.0%	15 (3) 33.3%	9 (3) 22.0%	15 (4) 32.6%
Lots sold for over USD 10m	2	1	3	4	11	16	23
... thereof guaranteed	1 * 50.0%	0 * 0.0%	2 (1) 66.7%	2 (1) 50.0%	6 (5) 54.5%	7 (6) 43.8%	15 (4) 65.2%
Total sales of guaranteed lots (in USD m)	48.1 42.3%	16.3 22.0%	80.0 29.3%	93.2 42.2%	185.1 44.9%	226.6 32.8%	521.7 61.2%
... thereof guaranteed lots over USD 10m (in USD m)	14.9 30.9%	0.0 0.0%	59.5 74.4%	59.5 63.8%	140.7 76.0%	189.4 83.6%	437.0 83.8%

Note: Unsold and retrieved lots not included in analysis
* Before 2010 Christie's did not make any distinction between third-party guarantees and in-house guarantees.

Table 1: Analysis of Christie's November Contemporary Evening Sales Auctions 2008-14

Sotheby's	2008	2009	2010	2011	2012	2013	2014
Total sales (in USD m)	125.1	134.4	222.5	315.8	375.1	380.6	343.7
Total lots sold	43	51	49	62	58	54	67
… thereof guaranteed	20 (0) 46.5%	0 (0) 0.0%	3 (3) 6.1%	11 (10) 17.7%	9 (7) 15.5%	12 (3) 22.2%	33 (12) 49.3%
Lots sold below USD 1m	9	24	4	17	15	10	14
… thereof guaranteed	4 (0) 44.4%	0 (0) 0.0%	0 (0) 0.0%	0 (0) 0.0%	0 (0) 0.0%	2 (2) 20.0%	8 (1) 57.1%
Lots sold for USD 1m - 10m	32	26	39	38	36	38	46
… thereof guaranteed	15 (0) 46.9%	0 (0) 0.0%	1 (1) 2.6%	8 (7) 21.1%	5 (3) 13.9%	6 (0) 15.8%	20 (8) 43.5%
Lots sold for over USD 10m	2	1	6	7	7	6	7
… thereof guaranteed	1 (0) 50.0%	0 (0) 0.0%	2 (2) 33.3%	3 (3) 42.9%	4 (4) 57.1%	4 (1) 66.7%	5 (3) 71.4%
Total sales of guaranteed lots (in USD m)	56.4 45.1%	0.0 0.0%	28.5 12.8%	138.5 43.9%	125.6 33.5%	154.9 40.7%	185.8 54.1%
… thereof guaranteed lots over USD 10m (in USD m)	10.2 18.0%	0.0 n/a	25.4 88.9%	112.8 81.4%	89.4 71.2%	129.1 83.3%	91.0 49.0%

Note: Unsold and retrieved lots not included in analysis

Table 2: Analysis of Sotheby's November Contemporary Evening Sales Auctions 2008-14

If we compare the development on the chart we see that the curve is increasing for both auction houses.

I made several observations looking at previously sold lots.

First, we see that the number of sold lots is generally increasing. Christie's sold 44 lots in 2008 compared to 75 lots in 2014 (+70%). Sotheby's sold 43 lots in November 2008 in comparison to 67 lots in November 2014 (+56%). The increased number of lots sold can be explained by the economic slowdown in 2008-2009.

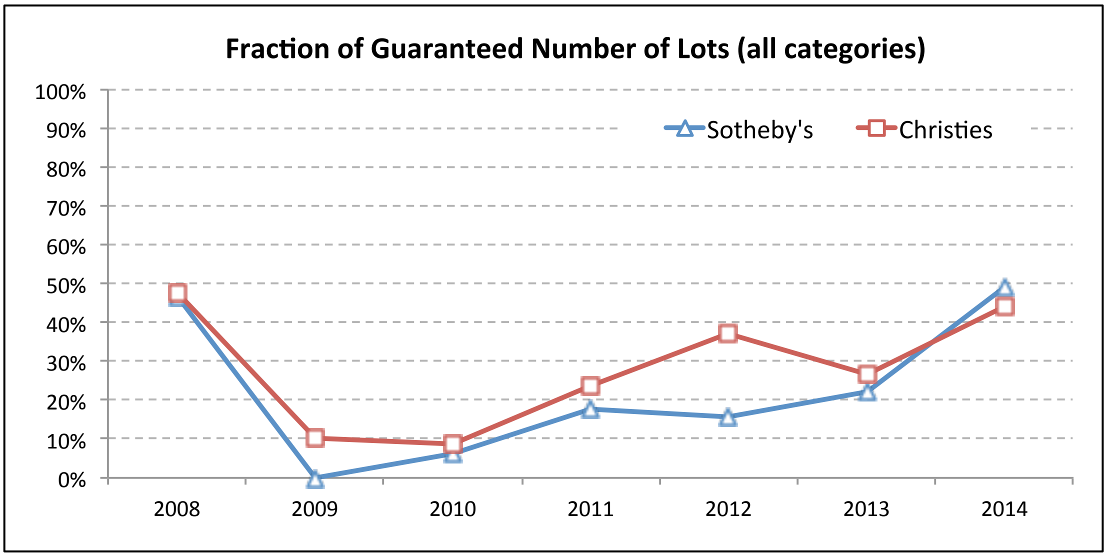
A brief analysis of the average sales prices, i.e. hammer prices including buyer's premiums, is even more interesting. At Christie's the average sales price increased from USD 2.6 million in 2008 to USD 11.4 million in 2014 (+340%). At Sotheby's the value increased from USD 2.9 million to USD 5.1 million (+76%). Therefore, the main driver for the increased sales volumes of these auctions seem to come from significantly higher bidding prices rather than from a higher number of offered artworks.

Secondly, a look at the distribution between the three groups of lot sizes (below USD 1 million, USD 1 – 10 million, above USD 10 million) might give some additional insights. Christie's turns out to be the better example for this question. The number of lots sold below USD 1 million is decreasing whereas the number of lots sold above USD 10 million is increasing auction by auction. The middle group with the lots sold between USD 1 to 10 million also follows a rather positive trend during 2008-2014. The development in the above 10 million group confirms the assumption that the contemporary art market is increasingly concentrating on high-end artworks.

Another observation concerns the guarantees. Chart 1 illustrates the development of the number of guaranteed lots relative to the number of total lots sold, Chart 2 shows the development of the guaranteed sales volume in relation to the overall sales volumes. The two lines in Chart 1 present very similar trends for the two auction houses: after the fraction of the guaranteed number of lots was at about 50% for both competitors, there was a significant drop to 0-10% in 2009 and 2010. The percentage values started to recover in

2011, and subsequently increased to the previous 2008 level of close to 50% in 2014. Taking a look at Chart 2 shows a partly similar picture. Sotheby's also had a clear drop in guaranteed sales volumes in 2009/2010 whereas Christie's fraction of guaranteed sales volumes did not change significantly. In 2014, both auction houses showed guaranteed sales volumes between 50% and 60% of total sales. In summary, auction sales guarantees show an increasing importance based on this analysis.

Illustration 1: Fraction of Guaranteed Number of Lots (all categories) Christie's and Sotheby's



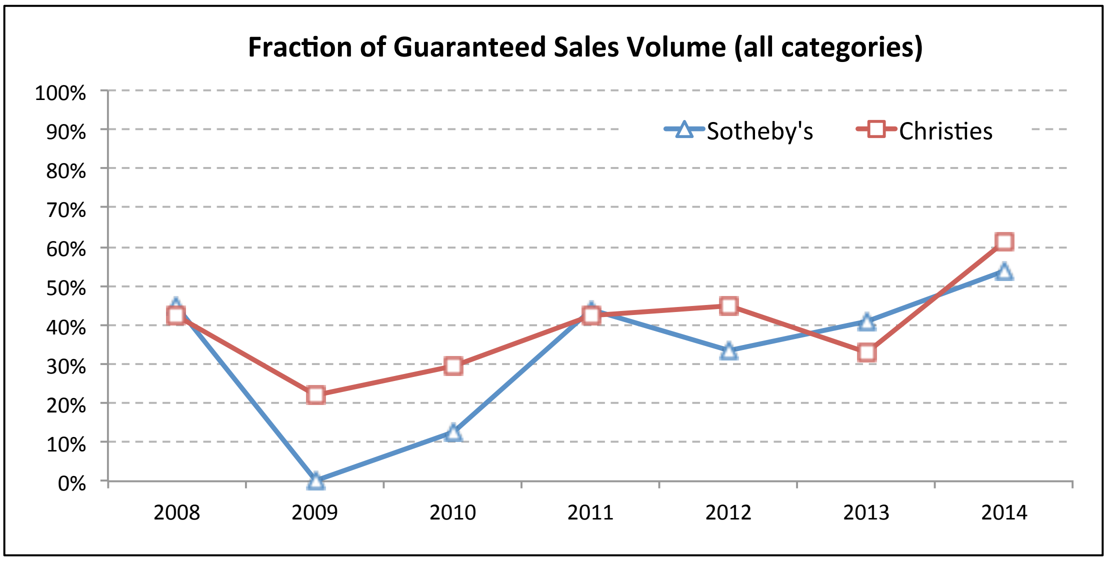


Illustration 2: Fraction of Guaranteed Sales Volumes (all categories) Christie's and Sotheby's

Charts 3 and 4 show the same analysis for the lots sold above USD 10 million. The insights are quite similar to the analysis with the overall sample (all guaranteed lots). Both auction houses experienced a drop to zero in

2009. However, the guarantees for lots sold above USD 10 million had already recovered by 2010, reaching a fraction above 70% of total sales volumes. A comparison between 2008 (Christie’s 31%, Sotheby’s 18%) and 2013/2014 (Christie’s 84%, Sotheby’s 49-83%) reveals a clear upward trend in the importance of guarantees in the top group consisting of lots sold above USD 10 million.

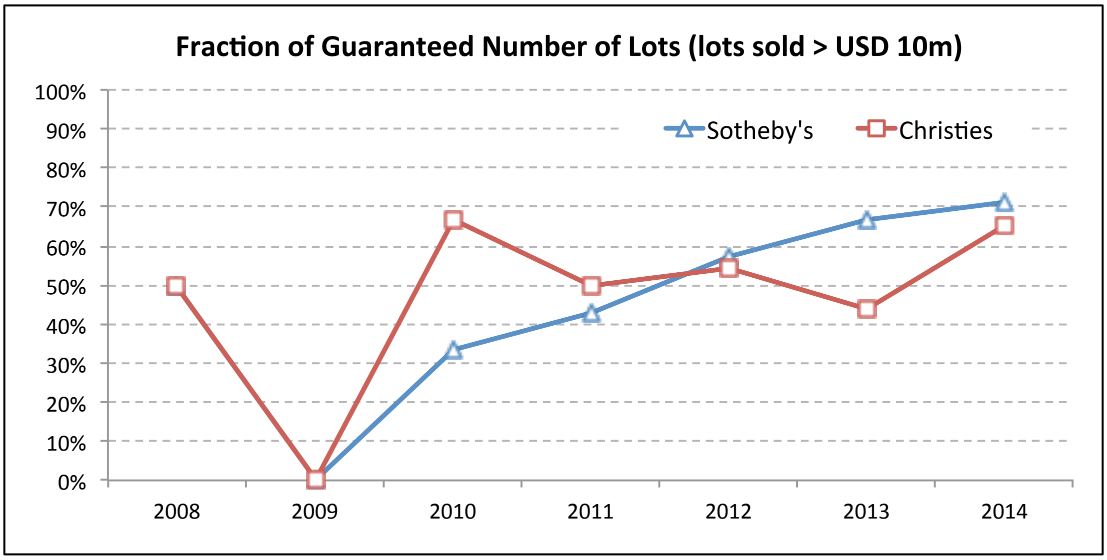


Illustration 3: Fraction of Guaranteed Number of Lots (lots sold > USD 10m) Christie’s and Sotheby’s

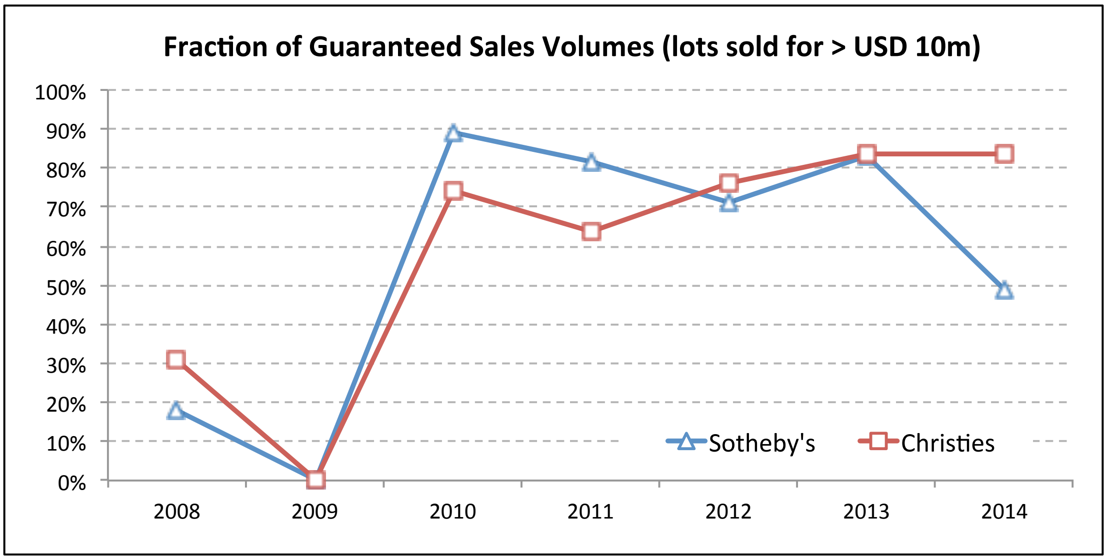


Illustration 4: Fraction of Guaranteed Sales Volumes (lots sold > USD 10m) Christie’s and Sotheby’s

It is difficult to evaluate the actual situation with third party guarantees, as there is no complete information available on this topic. Auctioneers are only required to disclose a guaranteed lot as backed by a third party if it is a “pure” third party guarantee. This means that it remains unclear for the rest of the guaranteed lots whether the guarantee was fully issued by the auction house or whether it was guaranteed together with a third party. The data shows that a substantial part of the guarantees were issued by third parties (Christie's: 9 out of 17 in 2013, 8 out of 33 in 2014; Sotheby's: 3 out of 12 in 2013, 12 out of 33 in 2014). In 2014, in both the section above USD 10 million and between USD 1 and 10 million, the auction houses guaranteed half of the lots and half were full third party guarantees. Compared to the number of third party guarantees at the Sotheby's November 2008 auction when there were no third party guarantees at all, it is evident that the auction houses are now increasingly trying to pass on the risk of guarantees to third parties (such data is not available for Christie's in 2008 and 2009). A logical explanation for this could be that the auction houses are trying to minimize their own risks in connection with auction guarantees.

To sum up this chapter, it is quite clear that guarantees have become more important for the two leading global auction houses. The analysis also shows that guarantees are especially important for backing the sales of the most valuable artworks in the contemporary art market. These trends might be supported by the fact that the average hammer prices at the Contemporary Art Evening Sales events have increased significantly during the last seven years.

6.4 Comparison to the Modern and Impressionist Auction Sales

Going further and taking a look at the Modern and Impressionist auction sales we can see that this market is still keeping its strong position, even if contemporary sales are the first runner. The Sotheby's auction results from February 2015 show very good sales in terms of lots sold. The February 2015 sales events from both auction houses, Christie's (GBP 80.3 million for 38 lots) and Sotheby's (GBP 170.2 million for 46 lots), brought together a sum of GBP 250.5 million. In these sales artworks were guaranteed. For the Christie's sale on 4 February 2015 only one lot was fully guaranteed by a third party. At Sotheby's the situation was different. According to the publicly available online auction catalogue, in the category of artworks between GBP

1 million to GBP 10 million, 6 were guaranteed – 5 by the auction house and one by a third party with the possibility of auction house involvement. In the category over GBP 10 million, 3 lots were guaranteed – one lot by the auction house directly and two by a third party with possible involvement from the auction house.

This Sotheby's sale took the highest ever takings for a sale of this kind (Modern and Impressionist Auction Evening Sale), with GBP 186.4 million worth of artworks being purchased and 85.3% of lots being sold.[159]

[159] Gleadell 2015 Colin Gleadell, *Guarantees Spur Sotheby's Impressionist and Modern Sale to Record £186.4 Million,* in Artnet News, on 4 February 2015, https://news.artnet.com/market/guarantees-spur-sothebys-impressionist-and-modern-sale-to-record-lb1864-million-241039, last access on 06.04.2015.

7 Case Studies

In this chapter I would like to show various examples of guaranteed lots in order to highlight the different outcomes and scenarios that are currently possible at main auction houses. Examples of artworks and information on the guarantees derive from publicly available sources.

7.1 In-house Guarantees

7.1.1 Lot Sold to the Auction House

There are several cases that are marked in the catalogue as 'lot owned by the auction house'. Sotheby's uses a triangle-sign with the following explanation behind the sign "Property in which Sotheby's has an ownership interest. Lots with this symbol indicate that Sotheby's owns the lot in whole or in part or has an economic interest in the lot equivalent to an ownership interest."[160]

An example of a lot owned / partly owned by the auction house is Andy Warhol's *Flowers (Five Foot Flowers)*, 1964, offered at the Sotheby's Contemporary Evening sale in New York on 13 November 2013.

We can assume that auction houses have a stock of such lots when they provide guarantees and several lots do not find a new buyer. In this case, the auction house pays the consignor the arranged guaranteed sum and gets the artwork in return. Now, owning these art pieces, the auction house offers them in a new auction sale trying to find new buyers.

The Sotheby's Annual Report also contains information concerning this fact, stating that "the inventory of the Agency segment consists principally of items obtained as a result of the failure of guaranteed property to sell at auction."[161]

7.1.2 Lot Sold to the New Buyer

[160] Sotheby's website, http://www.sothebys.com/en/auctions/ecatalogue/2013/nov-2013-contemporary-evening-n09037/lot.21.html, last access on 18.04.2015.
[161] Sotheby's 2014 Annual Report, p. 63.

A. Below the Guarantee Amount

Illustration 5: The Smooke Collection. Phillips Auction Sale on 5 November 2001

The guarantee provided by the Phillips auction house for the Smooke Collection is an important example of a guarantee given by an auction house. The whole collection offered for sale in New York on 5 November 2001 was estimated at approximately USD 80-100 million. However, the auction house gave a much higher guarantee to the owners in order to get the collection consigned. The guarantee sum was USD 185 million. The collection then sold pretty much at the low estimate – around USD 86.1 million. This is also an example where the whole collection was guaranteed, and not just a single lot.

The auction house experienced a huge loss, which led to the sale of the house to Simon de Pury later on.

B. At the Estimate

An example of a lot guaranteed by the auction house and which sold between both estimates is *Untitled* by Alexander Calder from 1946. Sotheby's auction catalogue for the Contemporary Art Evening Sale on 11 November 2008 in New York stated that the work had been guaranteed by the auction house. The auction estimate was between USD 1 - 1.5 million and the lot sold for USD 1,482,500. The catalogue entry contains a remark that the image is under artist's copyright.

If we consider that the auction house has guaranteed the lot somewhere between the low and high estimate, it does not get any percentage of the overage in this case as there would have been nearly no overage. Moreover, it is possible that it was pre-arranged that auction house had to share its buyer's premium with the consignor. However, the new trend of the auction houses is to keep the buyer's premium and not to share it with the consignor anymore.

C. Above the Guarantee Amount (and the Estimate)

In case the lot sells above the amount of the guarantee, there is an overage that could be shared.

Let's take the artwork *Nice 'N Easy* from 1999 by John Currin, which was offered in Sotheby's sale in November 2008. The lot was estimated at USD 3.5 - 4.5 million. It was guaranteed by the auction house and sold for USD 5,458,500, including the buyer's premium.

There are several possibilities as for the overage. For example, it can be arranged that the parties (auction house and the consignor) arrange that the upside will be split between the guarantor (auction house) and the consignor 30/70, meaning that 30% of the sum above the guaranteed amount goes to the auction house, and 70% to the consignor.

Another scenario for the overage is that the seller gets the "holiday", which means that a certain pre-discussed amount of the overage will go to the consignor. The auction house will then be entitled to participate in the overage as soon as the pre-discussed amount is reached. The percentage in this case could be 50-50% (instead of 30-70%) starting from a certain pre-discussed amount.

7.1.3 Lot Unsold

The idea of the guarantee is based on the belief that the lot will sell. However, looking at different results in the auction catalogues several guaranteed lots were not sold. Most probably these lots are pure auction house guarantee lots. The question remains as to how it is possible that they appear unsold in the auction catalogue and other databases.
An example from the last November sale is Andy Warhol's *Little Electric Chair,* which was offered at Sotheby's. If we look at Artprice.com we can see that the lot is marked as "Lot not sold".

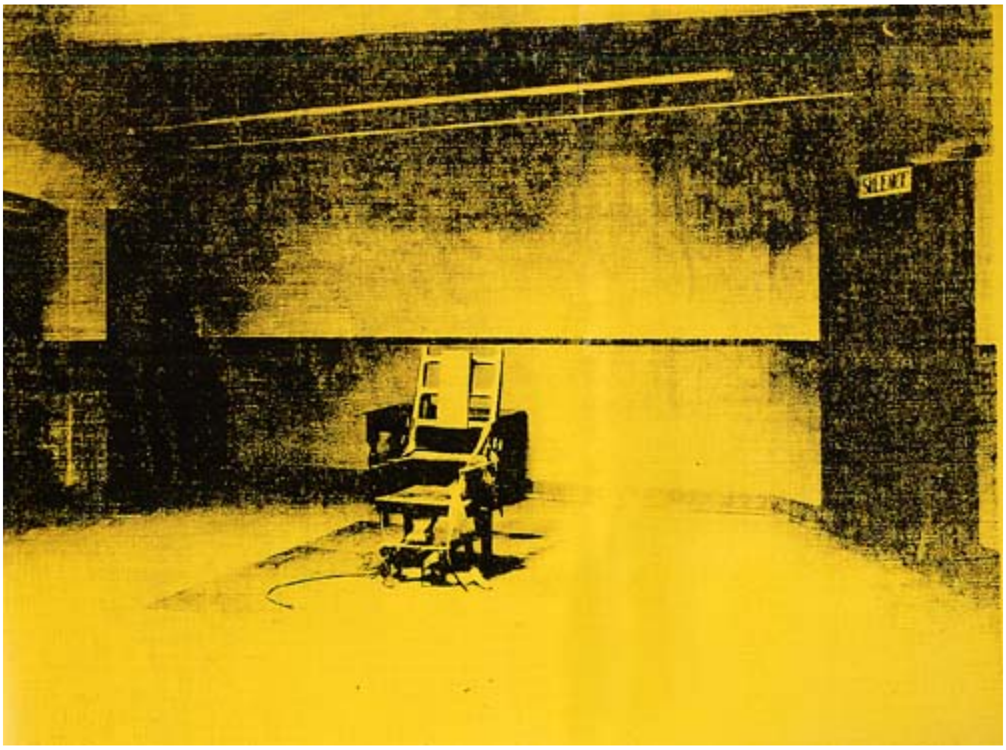


Illustration 6: Andy Warhol, *Little Electric Chair*, 1964

It was lot 37 from the Sotheby's Contemporary Evening Sale held on 14 November 2014 in New York (marked with the °-sign). *Little Electric Chair* by Andy Warhol was estimated at USD 7.5 - 9.5 million. Normally and according to the guarantee system there are no unsold lots. The idea of the guarantee is that the lot always sells.[162] It would be interesting to receive more information on this lot as this represents a controversy and an exception.
There is also another unsold lot in the same sale, which is Lot 33 (Jeff Koons, *Moon (Yellow)*, 1995-2000).
In contrast, Christie's was able to sell another similar artwork by Andy

[162] see also Thompson 2014, p.161 „...work with a guarantee is never passed..."

Warhol, *Little Electric Chair* for a price of USD 6,045,000 (estimated at USD 3.5 - 5.5 million) in the Contemporary Evening Sale held from November 2014 in New York.

7.2 Third Party Guarantees

7.2.1 Lot Sold to the Guarantor

A. Above the Guarantee Sum

Illustration 7: Roy Lichtenstein, *"I Can See The Whole Room!... And There's Nobody In It!*, 1961

Roy Lichtenstein's *I Can See The Whole Room!... And There's Nobody In It!(1961)* is an example of a lot fully guaranteed by a third party, which also sold to the third party for a higher sum than the guaranteed one. The lot was offered at Christie's Contemporary Sale in New York in November 2011. The estimate for the work was USD 35 million to USD 45 million. According to the publicly available information, the Qatari Royal Family gave the guarantee at USD 33.5 million.[163] The lot was sold for USD 43,202,500 including buyer's premium to the Qatari Royal Family.

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[163] Thompson 2014, p.162.

If we take into account that normally the auction house will agree on 70/30 split with the seller, the following calculation could be possible. 70% from the overage (in this case this is the hammer price minus the auction guarantee of USD 33.5 million) will be given to the seller. 30% will be split 50/50 between the auction house and the third party guarantor. Christie's should get 15 % and 15 % will go the third party guarantor, in this case to the Qatari Royal Family. Furthermore, they could have arranged that they will not pay any buyer's premium. However, today the trend is going in the direction of obliging the buyer to pay the buyers premium, and on other hand to agree with the auction house on a 60/40 split instead of a 50/50 split.

The critique about the sale of this artwork in publicly available sources was about the final price. Taking into account all the deductions that third party guarantor had, the final price for the purchaser (in this case guarantor itself) was much less than the price reflected in the online auction catalogue or on Artprice.com The final price is around USD 40 million instead of the reported USD 43,202,500 and in this case it would no longer have been a record for a Lichtenstein artwork at that time.[164]

B. At the Guarantee Sum and Below the Estimate

[164] Salmon 2011 Felix Salmon, *Why you can't always trust the auction results*, in Reuters.com, on 21 November 2011, http://blogs.reuters.com/felix-salmon/2011/11/21/why-you-cant-always-trust-auction-results/, last access on 16.04.2015; Roy Lichtenstein's "Ohhh... Alright...", 1964 sold in the Christie's Contemporary Auction Sale in November 2010 for USD 42,642,500.

Illustration 8: Jeff Koons, *Pink Panther*, 1988

Another example is when the artwork sells at the guaranteed amount but below the auction estimate.

Jeff Koons's *Pink Panther (1988)* was offered at Sotheby's Contemporary Art Evening Sales in New York in May 2011. The estimate was at USD 20 to 30 million. Apparently Benedikt Taschen consigned the piece for a guaranteed amount of approximately USD 16.8 million.[165] The guarantee sum was the same as the selling price. In this case the guarantor gets an artwork without getting any per cent of the overage as no overage was produced. Even if any overage would be produced and the guarantor gets the piece, s/he would most probably not profit from it, as was the case here at Sotheby's. According to Sotheby's rules, the guarantor does not get a finance fee (any share of the overage) in the case s/he wins the auction and finally buys the artwork.

It can also be that it was arranged that the buyer's premium would be dismissed by the auction house, or that the buyer (the guarantor in this case) would pay just a share of the buyer's premium. Normally the auction house gets the seller's and the buyer's premium. But it can also happen that the seller tries to avoid this premium. However, there is no real risk in this case for the auction house except for the possible costs surrounding promotion, marketing and other costs for the sale of this art piece. As for the third party investor, to take such a risk only makes sense if s/he really likes the piece

[165] Thompson 2014, p.162.

and would like to own it. As the piece went to a telephone bidder from China, one could suppose that the Chinese collector now owns this art piece.

7.2.2 Lot Sold to the New Buyer

A. Above the Estimate

Illustration 9: Andy Warhol, *White Marilyn*, 1962

Andy Warhol's *White Marilyn*, which was guaranteed, possibly partly through a third party, provides an example of a lot, which doubled the high estimate. *White Marilyn*, 1962 was sold for USD 41,045,000 at Christie's May 2014 Contemporary Evening Sale. The estimate was at USD 12 to 18 million. A Special Notice of the auction house contains the information that the lot was guaranteed. While we do not have exact information that it was a third party guarantee, we can assume it was.

Assuming that this lot was guaranteed at USD 16 million, the overage excl. buyer's premium (= USD 4.4 million) is around USD 20.6 million. In case the consignor gets 70% of the overage, he will get USD 14.4 million. In case the third party and the auction house agreed to equally split their 30% share of the overage, which is USD 6.2 million, each of them will get USD 3.1 million.

B. Lot Unsold

We must assume that this situation will not take place as we have a third party, who is obliged to buy the guaranteed lot against the guaranteed sum.

8 Outlook

In my opinion the auction guarantees system will continue to develop positively in the near future, with trends showing that the guarantee is increasing in use.
The overall volume and amount of art sales will be positive in the coming months.
Though the general art market outlook for 2015 was “moderate”, the Christie’s sale on Monday 11 May 2015 set a new record for a work by Pablo Picasso, *Femmes d’Algers*, 1955 which sold for USD 179.3 million including buyer’s premium. Interestingly, this artwork had been guaranteed.

As for the auction houses, guarantees represent a great opportunity to select and decide whether to guarantee the artwork in-house or to share the risk with an external third party. Especially for very high-end art works, auction houses should be able to better foresee and predict whether the lot can be sold with or without the involvement of the third party. Guaranteeing in-house and achieving good results would improve the auction house’s earnings.

As for the third party guarantors with profound background knowledge of the art market, making business through involvement in guaranteeing art works will remain an attractive way of participating in the art market. Especially taking into consideration the general sense of insecurity surrounding the current global economic situation, the instrument of the guarantee will remain a good alternative to traditional investment products.

The instrument of the guarantee represents a sign of the professionalization of the art market. In comparison to the financial industry with a great range of various products, the guarantee is a sort of an innovative art market instrument and a possible investment opportunity. Thus, the guarantees could be also interesting to new groups of potential investors in the future. New collectors or investors who are currently outside the art market could be involved in the art market generally and especially in the context of the external guarantees.

The development of transparency and regulatory issues are difficult to forecast. However, as seen in the financial industry in recent years, major changes in the art market, including surrounding guaranteed art works, could occur sooner than expected.

9 Conclusion

This paper set out to explore the guarantees system in the framework of the growing contemporary art market.
I concentrated on the phenomenon of the appearance of guarantees.
In the first part I analysed the historical background, outlined the definitions and possible legal settings. Furthermore, I made a distinction between pure guarantees and third party guarantees and had a look at the different parties involved, such as the consignor, the guarantor (auction house and/or third party) and the buyer. The ideas of the guarantee, and its potential advantages and disadvantages for each of these parties has been analysed.

In the second part of the paper I looked at contemporary auction sales at the two most important auction houses Christie's and Sotheby's from 2008 until 2014. I also illustrated several possible scenarios involving the guarantees in the case studies section.

Below I summarize the most important observations.

Firstly, the guarantees represent an innovative instrument within the auction practice. They are issued by the auction house directly or backed-up through third parties. After the economic crisis of 2008 there has been an increase in third party guarantees due to the strategic change at auction houses, which has seen them seeking to reduce risk.

Secondly, the number and volume of guarantees, both in-house and third party guarantees, is increasing year after year. This is a reflection of the reality of the contemporary art market. The art market is still confident and the volume of guaranteed lots confirms it.

Thirdly, guarantees are mostly used for high-end artworks. This is explained by the fact that a guarantee as a kind of insurance makes sense for the consignor, especially for the most expensive and valuable artworks. The estimated worth of guaranteed artworks seems to be high in comparison to similar artworks that are not guaranteed. This suggests that the valuation process for guaranteed works is performed differently than for non-guaranteed works.

Another finding is that guarantees still remain a relatively confidential topic. This phenomenon was discovered and confirmed in the course of this paper due to the unavailability of auction house experts' opinions to be included in the paper. Auction houses create a kind of mystery around their headline auction sales and it is possibly part of their business model not to explain their business strategy in a more open way. Thereby they can try to capture and maintain audience interest through the promotion of the art market as "mysterious".

The confidentiality issue brings me to the next finding, that of the transparency of the art auctions.

Auction houses pretend to be a fair and transparent platform for art sale and purchase. This is surely true if we think that it is the only art market player that makes its achieved prices public. However, this transparency is not given in the case of the third party guarantee as different classes of customers are created.

Although auction houses disclose certain information, there are still many open questions, such as what is the guarantee amount, who is behind it, which extra arrangements have been made, whether the third party will be present in the auction room and bid during the sale, etc. Moreover, the signs and/or notices that signal a guarantee are sometimes more perplexing than helpful. Is a certain lot now financed by the auction house or by a third party? And if the financing is by both, what is the share for the each of them? Maybe there are even more than two parties involved?

It is argued here that more regulation is required in the guarantees system given its limited fairness and uncertainty. A good start could be the regulation of the role and the behaviour of the guarantor during the sale. The situation is improved in the case that the guarantor does not have the right to bid, as s/he cannot heat the price and make it higher and higher. Clear regulation of and communication about the investor's role would be another good first step in regulating guarantees. More information behind the third parties guarantees, including the % of the guarantee and the parties involved would also be helpful. This would also improve the buyer's position.

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