



# Auctioning institutions in China: economic and legal aspects

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## Abstract

**Motivation:** China is now the third largest art market in the world, and thanks to its long history, the country is able to offer a great artistic heritage. Chinese auctioning institutions have become one of the most significant in the world, having a massive global impact on art pricing. By establishing their sales infrastructure in new locales ahead of the traditional mechanisms of primary market commercial galleries, the Chinese auction houses have played a foundational role in the notional construction of new genres of art.

**Aim:** The main purpose of this article is to present a detailed analysis of Chinese auction houses and other auction institutions, with regards to the economic and legal aspects of their operation. The article is cross-sectional, showing how China has become the fastest growing art market in the world. The analysis provides evidence for the existence of various factors that determine the dynamic development of the Chinese art auctions market and determines the differences in the functioning of Chinese and Western auction houses.

**Results:** These results illustrate that exceptional economic and political factors made it possible to significantly develop the Chinese auction market in a very short time.

*Keywords:* Chinese art market; auction houses; Chinese auction houses

*JEL:* ZI; R1

## 1. Introduction

The Chinese civilization has been around for over 5,000 years. The long history has left a significant artistic legacy behind it. Since its inception, the Chinese art

market has undergone many changes that correspond to the transformations of Chinese culture, from practicality to craftsmanship, from barter to the emergence of awareness of the commodity economy (Łakomska, 2015, p. 7). Collecting in China has a very long tradition, dating back to ancient times. During the Tang Dynasty, traditional Chinese paintings were collected, antique bronzes were collected during the Song Dynasty, but the real boom in the Ming Dynasty, when the first independent shops with paintings and calligraphy appeared. During the reign of the Qing Dynasty, Beijing and Shanghai became art trade centres. The number of works of art sold increased significantly, and along with their popularity, the number of cases of counterfeiting also increased (Li, 2017, p. 87). The reign of the Qing dynasty is also the first attempts to develop museology in China. Unfortunately, from the mid-nineteenth century to the present day, China has been systematically losing this priceless heritage, whether because of looting, illegal sale, or deliberate or accidental damage. Much of China's cultural heritage has been scattered around the world. In modern times, after establishing the so-called New China by Mao Zedong in 1949, trade in works of art ceased to be of significant economic and social importance. The Great Proletarian Cultural Revolution (1966–1976), during which art was considered socially harmful, and many priceless monuments, works of art and books were deliberately destroyed, constituting a significant turning point in the history of the Chinese art market. The cultural revolution for many years contributed to the recession on the art market, and its effects are still felt today both in the economic (lack of supply of some works of art) and social dimensions (respect for old traditions and monuments). Deng Xiaoping's reforms in the 1980s led to the opening of China to the world and the gradual development of the Chinese art market. For the first time in years, the public mood began to encourage collecting works of art. For the first time, we can also talk about the existence of the Chinese art market in the full sense of the word. The period of development of the Chinese art market can be divided into four phases: a period of transition, a period of growth, a period of adjustment and a period of comprehensive reconstruction:

- transition period (1980–1989);
- the period of growth (1990–2008);
- adjustment period (2009–2011);
- comprehensive construction period (2011–2014);
- stabilization period (2015–now) (Kamykowska, 2020)

The dynamic development of the Chinese art market in the last 30 years is a phenomenon on a global scale. Since 1992, the market has experienced three cyclical peaks in the years 1995–1997, 2003–2005 and 2009–2011, respectively. Currently, the Chinese art market is the second largest in the world in terms of volume and value of sales.

## 2. Literature review

Research on the art market focuses on 4 main perspectives. The first one examines the issues of valuing works of art. Hansmann and Kraakman (2002) emphasize the importance of politics and society in the valuation of works of art. Research by Hutter and Shusterman (2006) proves, however, that the economic value of a work of art is the greater the more varieties of value the work has in common. However, Dümcke and Matassa (2012) emphasize that the actual price of a work of art depends on how much the person is willing to pay.

The second perspective is the concentration of the investment nature of the art market. Baumol (1986) and Stein (1977) examine the return on investment in works of art by comparing it with the returns on risk-free assets (they indicate a lower return on investment in works of art). These findings challenge the study by Goetzmann (1993), which indicates that returns on art investments are higher than returns on UK stocks over the same period. This trend is continued by Mei and Moses (2002), who also conclude that the estimates of auction house prices are overstated, which has an impact on investors similar to the stock markets. Mandel (2009) also points to a higher return on investment in works of art compared to bonds. Emerging art markets, including China, appear in the broadcasts of Kraeussl and Logher (2010) as interesting investment opportunities.

Returns on investment in the art market are directly related to the notion of investment risk, which is the third perspective of art market research. Agnello's (2002) research focusing on American painting shows that works of art have twice the standard deviation of the SP500 index. Worthington and Higgs (2006), examining Australian art, noticed that the associated risk is comparable to the equity risk. An important aspect of investment in works of art, however, remains portfolio diversification (Renneboog & Spaenjers, 2013). McQuillan and Lucey (2016) note that investing in works of art is as risky as investing in capital.

The Chinese art market is relatively young, so there is a limited amount of research. The Chinese art market in terms of return on investment was studied by Hsieh et al. (2010), and these studies found that returns on 20th century Chinese modern art were higher than returns on stock markets. Xiong (2012) emphasizes the social dimension of the art market and the importance of social transformation, which resulted in an increase in demand for Chinese fine arts and calligraphy, and consequently also an increase in the prices of works of art. The national and patriotic nature of investment in works of art was also studied by Shi et al. (2017), who showed that they investigated whether investors were more inclined to invest in native works of art. On the other hand, Wang (2017) uses a hedonic regression analysis 12 701 in his research, proving that Chinese works of high value have higher expected returns and lower risk than cheaper works.

### 3. Methods

The method used is the formal-dogmatic method based on the analysis of legal acts directly regulating the trade in works of art on the art market in the People's Republic of China. The following legal acts were analyzed:

- the *Auction law of the People's Republic of China* (1997);
- the Law of the People's Republic of China on the protection of cultural relics (1982);
- the *Criminal law of the People's Republic of China* (1979).

The analysis of these legal acts is focused on showing the factors influencing the operational functioning and economic results of Chinese auction houses. The economic aspects were also based on Art Market Reports 2017–2019, Global Chinese Art Report as well as Chinese literature.

### 4. Legal aspects of Chinese art market

The legal regulatory aspects of the art market are one of the most important factors determining sales. Legislative issues related to trade in works of art can be considered on several levels, such as:

- regulations on the protection of monuments;
- regulations concerning auctions of works of art and the functioning of auction houses;
- regulations concerning the authenticity of works of art;
- regulation on the import and export of works of art;
- regulations concerning the taxation of works of art.

The cultural heritage of China is unique in the world works of art, characterized by extraordinary diversity and a long history. Unfortunately, from the beginning of the 19th century, the priceless treasures of Chinese culture were systematically destroyed as a result of armed conflicts, looting and illegal smuggling. Further problems in the field of the protection of works of art were brought about by urbanization and the progressive industrialization of Chinese cities (Gruber, 2008, p. 255), and the formation of the legal regime for the protection of cultural goods was very slow.

The first step to legally protect cultural heritage and works of art was the consolidation of a state obligation in the Chinese *Constitution* (2004) in 1982. *Law of the People's Republic of China on the protection of cultural relics* (1982) passed at the 25th Session of the CCP on November 19, 1982, defines what a cultural good is, imposes on the authorities the obligation to administer and protect cultural goods, establishes state ownership over yet undiscovered cultural goods, imposes the obligation to obtain a permit for the export of cultural goods. The Act also emphasizes that the ownership of cultural goods is passed down from generation to generation, and private property is also subject to state protection. The last aspect means in practice the transformation of private property into



state property (Cuno 2010, p. 95). This law was repeated many times in 1991, 2002, 2007 and 2013 (Huo, 2016, p. 3).

The *Criminal law* (1979) also plays an important role in protecting cultural heritage. The first criminal code of 1979 contained only two articles regulating offenses against cultural objects: Art. 173 on smuggling and Art. 174 deals with the deliberate destruction of cultural heritage. Subsequent amendments to the penal code were introduced successively in 1997, introducing 6 articles on crimes against the cultural heritage and increasing penal sanctions. The 2011 amendment to the Criminal Code significantly eased penalties for crimes against cultural heritage (Huo, 2013, p. 163)

The art auction market in China is regulated by the *Auction law* (1997), issued for the first time in 1997 and then amended in 2004 and 2015, adopted in order to unify the acts of auctions, maintain the order of auctions and protect the rights and interests of all parties in bidding activities. This document precisely defines what may be the subject of the auction, defining it as an object, merchandise or property rights owned by the client, with the exception of items whose sale is prohibited by law or administrative provisions. In addition, it obliges both parties to the transaction to complete formalities prior to sale at auction, including with regard to cultural monuments covered by the auction permit, the obligation to evaluate and obtain a permit issued by the department for cultural monuments at the auctioneer's place of residence. *Auction law* (1997) also defines the basic roles by defining the terms: auctioneer, auction company, client, bidder and vendee. Article 11 of the document also sets out the conditions for setting up an auction company. These are:

- having a minimum share capital of CNY 1 million;
- having a name, organizational structure, premises and statute;
- employment of auction sales specialists, appraisers and other employees;
- establishing the rules of auction trading in line with the provisions of this Act;
- compliance with the regulations of the State Council concerning the development of auctioning.

In order to obtain a business license, auction companies must be registered with the Administrative Division of Industry and Trade of Activities.

Chinese legislation also regulates the export of works of art. In the case of the export of cultural relics, it is necessary to obtain a travel license from the Administrative Department for Cultural Monuments within the State Council. Transport, mailing or export of cultural relics is also subject to customs control on the basis of a previously submitted application from the National Examination Database on the Import and Export of Cultural Monuments, operating under the SACH. An export license is required for the purchase of cultural relics at auctions and subsequent export. All works created after 1911 are subject to control according to lists of artists issued by the State Administration of Cultural Heritage (SACH). While these works of art may be freely sold domestically, exports are subject to prior inspection and approval by the appropri-

ate authorities. For other works of art that are not listed or classified as cultural monuments, the export of a reasonable number of works for personal use must be notified in advance to customs.

## 5. Economic aspects of Chinese art market

According to the statistics of the National Industry Information Management System of the Ministry of Commerce (2020), at the end of 2019, 8,013 auction companies and 248 additional branches were operating in China. Compared to 2018, 620 new enterprises appeared, which is an increase by 8.39%. In 2019, auction companies employed 60,412 employees, including 13,504 auctioneers, which is an increase of 1.39% compared to the previous year. Auction firms cover a variety of markets including real estate, automotive, agriculture, land-use rights, intangible assets, and cultural and art monuments.

The Chinese art auction market is strongly regionalized, with three art trading centres where most of the auction houses are located. Some of them coincide with the areas of special economic zones. These are:

- the Beijing–Tianjin–Hebei region;
- Hong Kong;
- the Yangtze River Delta region (McAndrew, 2019, p. 151).

In 2019, among 40 houses 19 auctions with the highest turnover came from Beijing, 9 from the Yangtze Delta region, and 7 from Hong Kong (Artnet & CAA, 2020)

Based on the data published in the Global Chinese Art Auction Market Report 2020 (Artnet & CAA, 2020), we can see that the highest prices of works of art are usually achieved at auctions in Beijing and Hong Kong, and less frequently in Hangzhou and Shanghai. The highest selling prices in 2019 were achieved by Beijing Poly International auction House — CNY 5.655.993.100, China Guardian auction House — CNY 4465760000, Sotheby's Hong Kong — CNY 3.518.566.216, Beijing Yongle Auction — CNY 3.306.000.000, Xiling Yinshe Auction CNY 2,379,695,000, and the difference between the first and sixth auction house on the list was almost twice as much.

In terms of the number of objects offered and sold at auctions, in 2020 the most works of art and antiques were sold at Xiling Yinshe Auction — 30 451 items, China Guardian — 22 353 items, Beijing Poly 9 974 items, Sun-gari International Auction 9 610 items and Beijing Rombon Auction 6,405 pcs. In the case of most auction houses, the number of offered objects does not differ significantly from the number sold, and the sales ratio is above 70%. Beijing Yi Dian Zhen Cang International Auction — 22.15%, Shanghai HongSheng Auction — 64.56% and Shanghai Jinart Auction — 38.55% show lower sales.

The Chinese art auction market consists of three main segments: Chinese Painting and Calligraphy, Ceramics and Antiques, and Contemporary Art. Chinese paintings, ceramics and antiques are the dominant force in auctioning, both in terms of quantity.



The transaction volume in the porcelain and ceramics segment in 2018 amounted to 20.27 billion. CNY, and the number of objects sold is 106,086 units. The most expensive item in this segment sold in 2018 was an enamel vase from the Qing era during the reign of Emperor Kangxi, sold for 190 million CNY. Data from 2021 shows that this segment is growing steadily in terms of transaction value as auctions for items over CNY 10 million have increased by 106.45% compared to 2020. Geographically, most porcelain auctions take place in Mainland China.

Oil painting as well as modern and contemporary art constitute the youngest segment of the Chinese art market. After a long period of adjustment, according to the data of the AMMA Monitoring Center, this segment has been showing an upward trend for a long time. In 2018, the turnover of this segment amounted to CNY 8.19 billion, and the number of works of art sold was 7,505 units. Three years later, in the first half of 2021 alone, turnover was CNY 6.502 billion. Geographically, the Oil Painting, Modern and Contemporary Art segments grew in almost all regions of mainland China and Hong Kong. In 2021, many works by Japanese, Korean and South-East Asian artists were also released on the market and met with the acclaim of collectors.

According to the published report by Art Basel, the online art and antiques market performed well in 2019, with a sales value of USD 6 billion in 2018, an increase of 11% compared to 2017 (McAndrew, 2019, p. 21). The 2018 Chinese Auction Market Statistics report published by the China Auction Industry Association shows that net online auction sales nationwide for the same year amounted to CNY 828 million, 2% of the global total. These data may indicate that the state of Chinese e-commerce in art is not yet very mature, but a tendency of increasing interest in mobile auctions has been observed for several years. The progressive digitization of Chinese society has led to the development of unique solutions tailored to the mobile client, consisting in creating separate, viral content spreading over social media channels (Whitler, 2019)

## 6. Conclusion

The *Law on the protection of cultural relics* (1982) and the *Auction law* (1997) strictly regulate the supply of items that can be sold at auctions. The law expressly stipulates that pre-Yuan cultural monuments may not be auctioned. The export and import of cultural monuments are also strictly controlled. Works of art created before 1949 (with some exceptions) of a specific historical value are not subject to auctioning and works of art and monuments created before 1911 cannot leave China. In addition, in accordance with the provisions of the *Law on the protection of cultural relics* (1982), it is forbidden to establish joint ventures between Chinese and foreign enterprises and stores selling cultural monuments that are wholly owned by foreign entities. Legal restrictions define significant differences between Chinese and Western auction companies, e.g. due to legal restrictions, foreign auction houses are not allowed to auction cultural mon-

uments in China and cannot take cultural monuments out of the country for auctions. Chinese legislation precisely defines what items cannot be auctioned, excluding stolen or smuggled items. The *Auction law* (1997) introduces the concept of “cultural relics illegally stolen as a result of historical events”. This term covers cultural objects unjustly plundered in the years 1840–1945. The cultural relics that are banned from selling and buying at auctions include:

- state cultural monuments, except those approved by the state;
- valuable cultural monuments in the collections of cultural institutions not owned by the state;
- wall paintings, sculptures and building elements belonging to the state immovable cultural monuments, except those which have been legally permitted to dismantle and which are not collected by institutional bodies collecting cultural monuments;
- cultural heritage acquired through illegal channels or resources.

The COVID-19 pandemic has had a significant impact in accelerating the legal transformation of art trading in China. During the annual “Two Sessions” in 2021 it was agreed:

- the need to create a public list of works of art;
- the need to expand the infrastructure of art trade and exchange centres (yishupin jiaoyi zhongxin), with the goal of reaching 1000 centres by 2025;
- strengthening vocational training for art dealers and brokers.

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