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Jörn Kruse*

The EC-US Trade Conflict over Film and Television Software

During the recent Uruguay Round film and television software was a major field of conflict between the United States and the European Community, and it is easy to predict that this will continue for the rest of the decade. Are the markets for film and television software really dominated by American productions? What are the key factors in international trade and competitiveness? Which elements explain American success in audiovisual production? Are the European trade barriers, such as television quotas and subsidies, effective with respect to cultural or economic objectives?

The American audiovisual industry has been very competitive and increasingly successful at the box office as well as in the television software market and currently enjoys a dominant position. European countries, and others, felt themselves challenged not only for economic reasons, but also for cultural ones. Governments all over the world and the European Commission reacted with different defensive measures against American imports, purportedly based on cultural arguments. Their protectionist effects clearly violate free trade and have therefore been attacked by the United States. The resulting trade conflict has not been settled and will emerge again when the new industrial policy of the EC that is currently under way becomes effective.

Complaints about American dominance in the motion picture and television markets have been common for many years. But does it really exist? Is it increasing or eroding? The most prominent early studies of the audiovisual world market were initiated by UNESCO. International trade and the imports and exports of 87 western, eastern and third world countries were analyzed for the years 1973 and 1983.¹ These analyses found that the production of internationally traded film and television software is concentrated in large and wealthy market-based countries, and especially in the United States. More than a third of all imported films originated in the USA. Thirty per cent of worldwide television broadcasting time consisted of imported software, while the American stations imported only 1-2 per cent of their broadcasted material. For western European television channels, 44 per cent of the imported software were productions from

the United States, which accounted for 10 per cent of total broadcasting time.²

Imports significantly vary between types of programmes (Cf. Table 1).³ Entertainment programmes, which account for a significant share of television time in most countries, have the highest import quotas, exceeding 50 per cent in Western Europe and Asia and more than 70 per cent in Canada and Latin America, but amounting to only 2 per cent in the United States.

More recent figures show an even larger American share. It is estimated that around one half of all the world's imported television software originates in the USA, and about 80 per cent of official box office revenues in countries where American movies are shown.⁴ The latter also applies to the European Community, as a Think Tank Study for the European Commission has estimated.⁵

¹ Cf. Tapio Varis: *International Flow of Television Programs, Reports and Papers on Mass Communication*, Paris (UNESCO) 1985. Cf. also Steven S. Wildman and S. Siwek: *International Trade in Films and Television Programs*, Cambridge (Mass.) 1988; André Lange and J.-L. Renaud: *The Future of the European Audiovisual Industry*, European Institute for the Media, Manchester 1989; Eli M. Noam and Joel C. Millonzi (eds.): *The International Market in Film and Television Programs*, Norwood 1993.

² Cf. Tapio Varis: *Trends in the Global Traffic of Television Programs*, in: Eli M. Noam and Joel C. Millonzi (eds.), op. cit., p. 3. This share is smaller for prime-time programmes, since American software is used to fill fringe hours.

³ The left-hand column for each area indicates each category's total programming share. The right-hand columns show the import quotas for these categories.

⁴ Cf. Scott Sochay and B. Litman: *Export Markets and the U.S. Motion Picture Industry*, in: *Journal of Media Economics*, 1992, No. 5, p. 32.

⁵ Cf. Think Tank: *Report by the Think Tank, Directorate General X*, Brussels 1994.

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Table 1

Programme Categories and Imported Software in Different Countries and Regions

	Western Europe		Eastern Europe		USSR		Asia		Latin America		Canada		United States	
	all %	imp. %	all %	imp. %	all %	imp. %	all %	imp. %	all %	imp. %	all %	imp. %	all %	imp. %
Entertainment	35	53	36	49	27	14	48	53	44	71	36	72	40	2
Informative	29	5	20	7	30	2	15	30	16	20	35	-	19	1
Educational	9	10	13	9	14	-	7	13	7	13	8	-	7	0
Cultural	6	12	12	21	15	4	3	6	2	14	8	24	6	9
Religious	1	11	-	-	-	-	2	9	1	18	2	28	3	-
Sports	8	36	10	43	9	32	10	28	5	18	3	-	4	2
Other	12	30	9	21	5	5	15	41	25	17	8	35	21	0

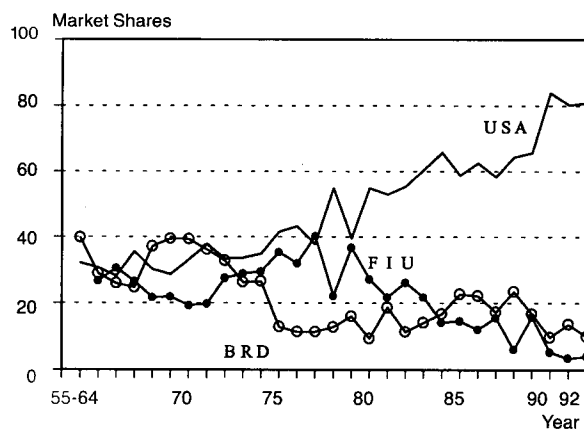
Source: Tapio Varis: Trends in the Global Traffic of Television Programs, in: Eli Noam and J. Millionzi (eds.): The International Market in Film and Television Programs, Norwood, New Jersey 1993, p. 7.

Table 2
Market Shares of Domestic and US Films in European Countries 1989-1992 in %

Country	US Films				Domestic Films			
	1989	1990	1991	1992	1989	1990	1991	1992
Germany	65.7	83.8	80.2	82.8	16.7	9.7	13.6	9.5
Belgium	69.5	73.4	79.6	72.9	2.6	3.8	3.1	4.2
Denmark	63.7	77.0	83.3	77.7	15.0	14.7	10.8	15.3
Finland	70.0	80.0	80.0	63.0	5.8	7.6	6.7	10.0
France	55.5	55.9	58.0	58.3	34.3	37.5	30.6	34.9
Greece	86.0	87.0	88.0	92.0	9.0	8.0	7.0	2.0
Ireland	75.0	87.0	91.5	-	2.0	5.0	2.0	-
Italy	73.0	74.7	-	54.4	17.2	18.9	-	-
Luxembourg	87.0	80.0	85.0	-	2.0	2.0	2.0	-
Netherlands	75.6	85.8	92.5	78.8	4.6	3.0	2.3	13.0
Norway	72.0	70.0	65.0	68.0	10.9	9.7	5.1	6.9
Portugal	81.0	85.0	85.0	-	1.0	1.0	1.0	-
Spain	73.0	72.0	69.0	77.1	7.3	10.4	10.0	9.3
Sweden	69.3	82.3	70.5	65.5	20.4	8.9	25.5	27.9
Switzerland	71.0	76.0	77.0	67.3	3.0	3.0	2.0	3.8
United Kingdom	84.0	89.0	84.0	-	10.0	7.0	13.8	-

Source: European Cinema Yearbook.

Figure 1
Countries of Production and Market Shares in Germany 1950-1992



FIU shows the accumulated figure for France, Italy and the United Kingdom.

Source: Hans G. Prodoehl: Filmpolitik und Filmförderung in Deutschland, in: Media Perspektiven, 1993, No. 4, p. 161.

While European films suffered a severe audience drop from 474 million customers in 1980 to 120 million in 1990 in European cinemas, the figure for American movies remained almost constant during that period with an audience of 420 million in 1990. Thus, American producers increased their market share.

The figures for the German market reflect this development during the last 30 years (cf. Figure 1). The market share of domestic productions dropped from 40 per cent as an average for the years 1955 to 1964 down to 10 per cent in 1992. Motion pictures from the major European production countries, France, Italy and the United Kingdom, used to have a combined market share of 25 per cent and ended with less than 5 per cent, while the Americans were able to raise their share from 30 per cent to 80 per cent. The result is comparable with other European countries, as Table 2 shows. With the exception of France and Sweden, American movies often account for 70-80 per cent, while domestic films usually achieve less than 15 per cent. At the end of the sixties, European cinema films accounted for 7-8 per cent of the American market. Today, the European share is 3 per cent, two percentage points of which are due to British films.⁶

The main reason for these sales figures is that top American pictures attract a much larger audience. While total sales have been around 80 per cent, "only" 50 per cent of all individual films shown in German cinemas from 1989 to 1992 have been American productions. Out of the ten most successful films in different countries in 1992, in Germany and Italy nine were American, in France five and in the United Kingdom ten.

Movies are not only shown in cinemas, but also, and increasingly important, on the television screen, where

⁶ Cf. Think Tank: Report by the Think Tank, Directorate General X, Brussels 1994, p. 28. The number of film imports into the United States slipped from 324 in 1970 to 140 in 1990.

Table 3

Movies on German Television 1992 and Countries of Production

Production Country	Public Service Television Stations			Commercial Television Stations					Σ	%
	ARD	ZDF	Other	RTL	SAT1	PRO7	Premiere	Other		
Germany	90	123	315	214	307	230	148	277	1704	12.46
Australia	1	2	18	3	—	11	53	17	105	0.77
Austria	5	3	20	8	75	62	—	34	207	1.51
Canada	2	4	19	10	3	12	75	18	143	1.05
France	56	45	294	48	29	91	260	204	1027	7.51
Italy	37	40	203	77	60	153	120	223	913	6.68
Spain	2	2	17	8	2	12	42	15	100	0.73
Sweden	—	5	48	—	1	2	122	27	205	1.50
United Kingdom	36	33	242	50	58	277	109	385	1190	8.70
United States	284	264	920	446	343	1299	2247	1173	6976	51.02
Other	44	103	540	50	88	28	115	136	1104	8.07
Total	557	624	2636	914	966	2177	3291	2509	13674	100

Source: SPIO (1993): Filmstatistisches Taschenbuch 1993, p. 59.

they make up one of the most popular types of programme. The numbers of motion pictures shown on German television in 1992 are listed in Table 3. Only one out of every eight films was a domestic production, while more than every second one originated in the United States.

Factors of Competitiveness

The empirical evidence shows that American audiovisual software is indeed very successful in different countries. United States producers hold a dominant position in several foreign motion picture markets and are very strong in television software. What are the reasons for American competitiveness in the international audiovisual markets?

Two basic economic characteristics of world trade in this industry should be mentioned first. Film and television production includes the creative process of generating the master of a specific software unit. Its costs do not depend on the number of copies made later on. The services being traded in the relevant markets are the legal rights to use the software, which are specified by different types of media (cinema, video, pay-television, free television etc.), by the region and by the period of time (and the frequency of usage). Thus, the most prominent economic characteristic of audiovisual services is non-rivalry in consumption. It infers that the marginal cost of supplying an existing software unit to other countries is zero.⁷ Viewed from the

supply side, a "natural world market" for audiovisual software seems to exist. Export incentives are strong.

But regional consumers' preferences may differ. The concept of a "cultural discount" refers to the fact that the audience in each country prefers local or domestic stories, settings, characters and actors to those from abroad. Thus, the audience size and sales figures of a specific imported unit are *ceteris paribus* diminished by a specific percentage.⁸ If this were very high for most pictures and television programmes, demand for imports would be low, the relevant audiovisual markets would be separated into national entities and international trade would not be relevant in economic and cultural terms. The degree of cultural discount varies among individual units and among the countries involved.

The main reasons for the tremendous business success of the American audiovisual production industry may be summarized in four points:

- The American motion picture and television industries have primarily been fields of business from the very beginning. The markets were typically ruled by fierce competition, the objectives were profit oriented, and success was closely related to mass audience attraction. As a result, a high level of overall professionalism in production and marketing has evolved. Entertainment is of outstanding importance.
- Due to the cost implications of non-rivalry, the

⁷ This does not include the costs of copying or dubbing, nor the costs of the distribution and consumption infrastructure. Because of the legal character of software rights, cross-border arbitrage is impossible for customers, leaving illegal usage aside. Thus, pricing in one national market is independent from pricing in other countries. See below.

⁸ For the concept of cultural discount cf. Colin Hoskins and R. Mirus: Reasons for the U.S. Dominance of the International Trade in Television Programs, in: Media, Culture and Society, 1988, No. 10, pp.499-515; Björn Frank: A Note on the International Dominance of the U.S. in the Trade in Movies and Television Fiction, in: Journal of Media Economics, 1992, No. 5, pp. 31-38.

outstanding determinant of profits in the audiovisual production business is consumer attraction, while total costs and prices are almost secondary issues.⁹ An important empirical consequence has been the growth of production budgets, which have tripled since 1980 (cf. Table 4),¹⁰ as far as motion pictures by Hollywood's major studios are concerned. Another business reaction to unit cost depression is massive advertising. Since these outlays are highly sunk investments and consumer attraction is very uncertain, audiovisual production is a risky business.¹¹ Three out of four productions may not cover total costs,¹² while outstanding pictures may reap hundreds of millions of dollars at the box office in only a few weeks. The adequate supply of risk capital is therefore of major importance and has been a primary reason for Hollywood's business success.

□ The structure of the American audiovisual industry is highly competitive and vertical integration is low due to economic efficiencies as well as to antitrust policy. The prevalence of project oriented contracts for the creative personnel and the existence of markets for specialized inputs allow for efficient and high quality production by incumbents as well as newcomers, whose entry barriers are low. Film and television production is highly concentrated in Los Angeles. This allows the significant agglomerative cost efficiencies which attribute to the audiovisual sector to be taken advantage of. Regional concentration itself is a prerequisite for vertical disaggregation.

⁹ Unit costs per customer are only relevant as *ex post* figures. They are not helpful for decision-making purposes. The variation of prices for software rights in the syndication markets solely depends upon the quantitative component (observed or expected audience size).

¹⁰ Cf. Scott Sochay and B. Litman: Export Markets and the U.S. Motion Picture Industry, in: Journal of Media Economics, 1992, No. 5, p. 36; and Variety of March 14, 1994.

¹¹ At the time of production decision-making, audience size is largely uncertain, even for the major studios' experts. There were quite a number of expensive failures, as well as remarkable successes by projects which had been rejected as unpromising by several studios.

¹² Two out of three new television series were cancelled by the networks after several weeks because they failed to attract a large enough audience. Cf. R. Lewine, S. Eastman and W. Adams: Prime Time Network Television Programming, in: S. Eastman, S. Head and L. Klein: Broadcasting/Cable Programming, 2nd ed., Belmont 1985; Harold Vogel: Entertainment Industry Economics, Cambridge (Mass.) 1986.

¹³ Due to cultural discount, it pays more to spend an extra dollar on quality the larger the domestic audience is. This secondary effect of increased budgets more than outweighs the primary effect of the cultural discount. Therefore, the cultural discount is not a handicap for US productions; indeed, the contrary holds. Cf. Björn Frank, op. cit.

¹⁴ Larger markets will typically exhibit a higher degree of heterogeneity. This creates incentives for products that attract audiences across cultural segments. Cf. Colin Hoskins and R. Mirus, op. cit.; Stephen Wildman and S. Siwek: International Trade in Films and Television Programs, American Enterprise Institute, Cambridge (Mass.) 1988. Colin Hoskins, R. Mirus and W. Rozeboom: U.S. Television Programs in the international Market: Unfair Pricing?, in: Journal of Communication, 1989, No. 39, pp. 55-75.

Table 4

Average Production Costs for Movies by US Major Studios

Year	Average Costs of Production			Average Costs of Marketing
	Million US\$	% Growth per Year	Growth accumulated	Million US\$
1980	9.3	—	100	4.3
1981	10.0	7.5	108	—
1982	11.3	13.0	122	—
1983	11.8	4.4	127	—
1984	14.4	22.0	155	—
1985	16.8	16.7	181	7.2
1986	17.5	4.2	188	6.7
1987	20.1	14.9	216	8.0
1988	18.1	-10.0	195	8.4
1989	23.5	29.8	253	9.2
1990	26.8	14.0	288	11.6
1992	28.9	—	311	—
1993	29.9	3.5	322	14.1

Sources: Scott Sochay and B. Litman: Export Markets and the U.S. Motion Picture Industry, in: Journal of Media Economics, 1992, No. 5; and Variety, March 14, 1994.

□ Their large domestic market is a major advantage for American productions. While a significant cultural discount may be viewed as a natural barrier against dominance in foreign markets it is even more a disadvantage for smaller countries. Combined with the cost structure implications of non-rivalry and the tendency towards higher budgets,¹³ cultural discount is a competitive advantage for producers in large and rich home markets like that of the USA.¹⁴ Additionally, American producers have the advantage of the English language, which practically enlarges their home market and cultural neighbourhood.¹⁵

It has been argued that the American market position was due to unfair practices,¹⁶ especially the strategic use

¹⁵ Imports are generally higher if the exporting country has the same language. The gross national product of the English-speaking countries is four times the GNP of the next largest language areas, German and Japanese. Additionally, English is very important as a second language in many countries, which allows the saving of dubbing costs in smaller foreign markets. Cf. Steven Wildman and S. Siwek: The Economics of Trade in Recorded Media Products in a Multilingual World: Implications for National Media Policies, in: Eli M. Noam and Joel C. Millonzi (eds.), op.cit., p. 25; André Lange and J.-L. Renaud: The Future of the European Audiovisual Industry, European Institute for the Media, Manchester 1989, p. 283.

¹⁶ Cf. for these arguments Jean-Luc Renaud: International Trade in Television Programs: Quota Policies and Consumer Choice Revisited, in: Eli M. Noam and Joel C. Millonzi (eds.), op.cit., pp. 151-161, and for a discussion of them Colin Hoskins, R. Mirus and W. Rozeboom, op. cit.; Keith Acheson, C. Maule and E. Filleul: Folly of Quotas on Films and Television Programs, in: World Economy, 1989, No. 12, pp. 515-524, here p. 519; Eli M. Noam: Media Americanization, National Culture, and Forces of Integration, in: Eli M. Noam and Joel C. Millonzi (eds.), op.cit.; Michael Tracey: A Taste of Money: Popular Culture and the Economics of Global Television, in: Eli M. Noam and Joel C. Millonzi (eds.), op.cit.

Table 5
Television Software Prices of American Productions in European Countries

	Prices in 1,000 US\$				Prices in US\$ per million Inh.			
	Series per one-hour Episode		Theatrical Movies		Series per one-hour Episode		Theatrical Movies	
	from	to	from	to	from	to	from	to
Austria	1.0	3.0	6.0	8.0	128	385	769	1,026
Belgium	7.0	9.0	5.0	21.0	707	909	505	2,121
Czechoslovakia	0.7	1.5	—	2.0	45	96	—	127
Denmark	2.5	3.0	4.0	7.5	490	588	784	1,471
Finland	2.2	3.0	4.5	10.0	440	600	900	2,000
France	25.0	50.0	30.0	150.0	442	883	530	2,650
Germany	12.0	46.0	22.5	175.0	152	582	285	2,215
Greece	0.9	1.1	3.0	3.7	88	107	292	361
Hungary	1.2	1.3	—	1.5	115	125	—	144
Iceland	0.5	0.7	0.5	1.0	1,923	2,692	1,923	3,846
Ireland	1.0	1.0	3.0	6.0	286	286	857	1,714
Italy	10.0	30.0	20.0	750.0	173	520	347	12,998
Netherlands	5.0	7.0	5.0	15.0	333	467	333	1,000
Norway	1.9	2.1	3.5	7.0	447	494	824	1,647
Poland	0.9	1.2	—	1.7	24	31	—	45
Portugal	1.5	1.7	1.2	2.0	144	163	115	192
Spain	7.0	20.0	30.0	1,000.0	179	510	765	25,510
Sweden	3.7	6.0	10.0	40.0	430	698	1,163	4,651
Turkey	1.6	2.2	—	3.0	28	39	—	53
United Kingdom	15.0	100.0	50.0	2,000.0	261	1,742	871	34,843

Source: Variety, April 6, 1992, p. 42.

of marginal cost pricing. This did not allow domestic producers to compete with American imports. Indeed, prices for American software were low in a number of countries for a long time.

In order to evaluate this argument, it is important to recognize that software prices in one country are independent of those in other countries. This is due to the fact that the traded entity is the specified right to use the software in that particular country and, therefore, cross-border arbitrage does not occur. As Table 5 indicates, price ranges (in absolute dollars as well as in dollars per million inhabitants) vary significantly among countries. This is due to income levels, specific preferences, market structure on the demand side and aggregate demand in the individual country.¹⁷

If the number of television channels and, therefore, the aggregate demand for software is small, or the demand side is monopolistic (both of which applied to most European countries until the 1980s), prices can be

expected to be low. Accepting low prices is the profit maximizing strategy for software sellers (syndicators), since marginal costs are zero.¹⁸ Predatory pricing would not be a rational strategy for a single American producer, since he would not be able to reap the benefits later because the supply side is competitive and entry barriers are low.

The American success basically accrues to superior products and efficient production and marketing. Over the years, American movies and television programmes have developed a goodwill for attractive entertainment, making contemporary success a result of earlier achievements. This includes the popularity of movie stars, who are very important for a picture's success. The effect of goodwill not only applies to the audiences' decisions, but also to distributors, cinemas and television software buyers.

Cultural Objectives and Trade Barriers

American business success and international market dominance in film and television software has been attacked by the importing countries on two grounds. The official line concentrates on cultural arguments, which include the objective of preserving the cultural identity and heritage of the individual importing country.¹⁹ Some

¹⁷ For factors influencing international software prices cf. Colin Hoskins, R. Mirus and W. Rozeboom, op. cit.; André Lange and J.-L. Renaud, op. cit.; Stephen Wildman and S. Siwek: International Trade in Films and Television Programs op. cit.; Michael Dupagne: Factors Influencing the International Syndication Marketplace in the 1990s, in: *Journal of Media Economics*, 1992, No. 5, pp. 3-29; David Waterman: World Television Trade: The Economic Effects of Privatization and New Technology, in: Eli M. Noam and Joel M. Millonzi (eds.), op. cit., p. 73; Eli M. Noam: Media Americanization, National Culture, and Forces of Integration, in: Eli M. Noam and Joel C. Millonzi (eds.), op. cit.

¹⁸ It is assumed that the costs of dubbing, subtitles etc. are borne by the buyer.

¹⁹ Cf. Jean-Luc Renaud, op. cit.; Keith Acheson, C. Maule and E. Filleul, op. cit.

countries argue that defensive measures are necessary against entertainment oriented products that are regarded as culturally mediocre. Secondly, domestic producers, actors and other input factors suffer revenue and income losses. They typically use cultural arguments to obtain protectionist measures against American imports from their governments. It is plausible in the context of the political economy of market intervention that they are very often successful.

Countries all over the world are applying trade barriers in audiovisual services, including quantitative import restrictions, tariffs, subsidies, television quotas, control of revenue streams, and a variety of specific rules. Most of them are specifically designed to hinder American imports.²⁰

The most significant protectionist instruments that have been heavily disputed are television quotas. They define the minimal proportion of television channels' broadcasting time that has to be filled with domestic productions. Such quotas have been used in Canada for a long time. The Canadian Content Rules are specifically intended as restrictions on programme imports from the United States.²¹

The European Council's Directive of October 3, 1989 which followed the Green Paper "Television without Frontiers", imposed television quotas on the European level and opened a new round of controversy between the United States and the European Community. The directive, which has been most heavily advocated by the

French government, rules that broadcasters in the member states shall reserve more than half of transmission time for European productions. Since the time appointed to news, sports, events, games, advertising and teletext services is excluded from the overall transmission time, the quota primarily applies to feature films and entertainment series, which are the relevant imports from the USA.

Some of the member states had television quotas in their national broadcasting legislation prior to the directive and some increased them afterwards. In France, 60 per cent of programming time had to be European productions and 50 per cent had to be French, when a government decree in 1990 determined that 60 per cent of programming between 6 p.m. and 11 p.m. had to be produced in a Community state.²² In the United Kingdom, the "proper proportion" of European productions (1990 Broadcasting Act) has been interpreted as 75 per cent of total programming time. Italy's 1984 law required 40 per cent; this was increased to 51 per cent in 1994. Spain's television law of 1988 required that 55 per cent of programming (and 40 per cent of televised feature films) had to be of European origin. Portugal, the Netherlands and Germany did not have any content rules. Although originally Germany and Portugal also opposed the quota rules, Belgium and Denmark were the only states that actually voted against them.

The first report on the application of the directive reveals that the European share is far beyond the quota for most of the established channels,²³ a selection of which are shown in Table 6. But the EC quotas may be a restriction for new or movie oriented channels and for some foreign language channels for national or cultural minority groups.

Like other quantitative trade barriers, quotas are responsible for inefficiencies and the suboptimal use of

Table 6

**European Production's Share of Programming
as Defined by the EC Directive**

Country	Channel	1991	1992
Germany	ARD	88.10	90.10
	ZDF	79.40	80.90
	SAT 1	50.90	53.40
	RTL	45.00	49.00
	PRO 7	34.10	34.10
France	FR 2	76.30	74.80
	FR 3	83.00	76.90
	TF 1	70.70	66.00
	M 6	63.80	63.20
United Kingdom	BBC-1	—	71.50
	BBC-2	—	70.00
	ITV	—	65.40
	Channel-4	—	67.30
Italy	RAI-1	73.00	73.00
	RAI-2	58.00	61.00
	RAI-3	75.00	67.00
	Rete-4	27.00	39.50
	Canale 5	57.80	72.00
	Italia-1	42.50	39.80

Source: Memorandum from the Commission to Parliament and the Council on the Application of Articles 4 and 5 of Directive 89/552/EEC Television without Frontiers (1994), Statistical Summary.

²⁰ For a list of anti-American trade barriers in different countries in the 1980s see Stephen Wildman and S. Siwek, *op. cit.*, p. 100.

²¹ Cf. Keith Acheson, C. Maule and E. Filleul, *op. cit.*; Keith Acheson and C. Maule: Canadian Content Rules for Television: Misleading Lessons for Europe, in: *Journal of Cultural Economics*, 1992, No. 16, pp. 13-23; C. L. Anderson: Canadian Content Laws and Programming Diversity, in: *Canadian Public Policy*, 1992, No. 18, pp. 166-175. Whether a specific production is considered Canadian is decided on the basis of a point system, defining points for writer, director, highest paid actors, director of photography and others.

²² For television quotas in EC member states cf. Clint Smith: *International Trade in Television Programming and GATT: An Analysis of Why the European Community's Local Program Requirement Violates the General Agreement on Tariffs and Trade*, in: *International Tax and Business Lawyer*, 1993, No. 10, p. 107.

²³ Cf. Memorandum from the Commission to Parliament and the Council on the Application of Articles 4 and 5 of Directive 89/552/EEC Television without Frontiers (1994). Since the figures in the memorandum are based on the member states' reports, which mostly used the information from the individual channels, their reliability may be questionable.

international resources. Particularly, as far as quotas affect a channel's programming, they intervene in consumer preferences and prevent the considerable savings that are possibly exhaustible because of the global non-rivalry in the consumption of audiovisual software.

Are quotas effective for cultural objectives? In general, a domestic television programme's being produced instead of a barred import does not guarantee that its cultural value is superior to that of American productions. As long as channels compete, quotas may well affect the supply of programmes but not so much actual consumption, which depends on consumers' choices. Additionally, broadcasting stations can easily comply with overall quotas on television time without its having any effect on prime-time programming. While prime-time programming is most important, quota productions may be shown in fringe hours.

While the cultural value of television quotas is questionable, it is important to note that they will definitely increase demand for domestic productions, which is in the interest of producers, actors and many other input factors. And this is exactly in line with the protectionism in other industries.

Numerous countries pay subsidies to their national film industry. Principally, this can be justified with the economic concepts of externalities and merit goods, analogous to government subsidies for theatres, museums and other institutions of art and culture. This requires that funds are given on the basis of cultural criteria. Some subsidies comply with this requirement. Others pursue business success on national and international markets. These subsidies are comparable to those for agriculture or coal-mining.

Are film production subsidies effective in terms of cultural or economic objectives? The degree to which cultural goals have been reached can, to a certain extent, only be determined by subjective judgement. Most comments from the cultural and professional community do not indicate that much has been achieved. Economic objectives can be measured in terms of audience sizes and market shares in domestic and foreign markets, if not in profit rates. Most of the subsidized movies simply did not attract a large enough audience. For example, during 1985-1991 90 per cent of all German movies were seen by

less than 130,000 people and one half of the productions did not even make it to the box office, because distributors were not interested.²⁴

Film subsidies already existed during the period when European productions lost market shares to American productions (cf. Figure 1).²⁵ Since production cost differences are not the most relevant issue for a film's consumer attraction (and government aid is low compared to US film producers' budgets), subsidies cannot be expected to have much influence on the competitiveness of the domestic audiovisual production industry.

While some argue that subsidies were not successful enough, others assume that subsidization contributed to failure. The decision-making by commissions comprised of politicians, bureaucrats and insiders, and a mixture of cultural and economic criteria, provided the wrong incentives and created a mentality of subsidy-seeking among producers, which has been favourable neither to the cultural level nor to market success.

In addition, film-subsidy institutions are numerous. In Germany alone, there are 22 institutions,²⁶ the majority of which (the individual Länder) are designed to attract production into a specific region. This prevents the regional concentration of production which would be necessary to exploit agglomeration economies and to allow the development of efficient intrasectoral structures, thus reducing competitiveness. The same problem has been identified by the Commission in Brussels for the European level as one of the major reasons for the failure of European film policy.²⁷

The GATT Conflict

Despite trade barriers, film and television production is one of the most successful American export industries.²⁸ The revenues of motion pictures from major countries increased by 25 per cent per annum between 1985 and 1990. The export share of the American major studios' total revenues has increased from a third to almost one half since 1984.²⁹ Of the United States' television software exports, Europe accounts for nearly one half.

Since exports in general and the European market in particular have become more important, the Motion Picture Association of America protested against the EC quota directive and lobbied the Bush administration to

²⁴ Cf. Think Tank, *op. cit.*

²⁵ Cf. *ibid.*

²⁶ For a list of film-subsidizing institutions in Germany and their funds cf. Hans G. Prodoehl: *Filmpolitik und Filmförderung in Deutschland*, in: *Media Perspektiven*, 1993, No. 4, p. 165.

²⁷ Cf. European Commission: *Strategy Options to Strengthen the European Programme Industry in the Context of the Audiovisual Policy of the European Union*, Green Paper, Brussels 1994; Think Tank, *op. cit.*

²⁸ The trade balance of \$ 2.5 billion was topped only by the aircraft and space industry.

²⁹ Cf. Scott Sochay and B. Litman, *op. cit.*, p. 31.

invoke section 301 of the Free Trade Act.³⁰ The US trade representative filed a formal complaint with the GATT and threatened to take retaliatory action against European exports.³¹ Consultations with the European Commission failed to settle the dispute.

During the trade negotiations of the GATT Uruguay Round the United States sought to fully apply the rules of the "General Agreement on Trade in Services" (GATS) to audiovisual services. The European quotas would thus have been illegal and would have had to be removed. The position of the European Union was to include a permanent general exemption for cultural affairs. To obtain American consent, they offered not to increase quota protection, which was not accepted by the USA.

Formally, the audiovisual sector is included in the GATS agreement. But the "Final Act" includes the following provisions for audiovisual services:³² the most-favoured-nation-clause will not be effective; market access and national treatment obligations will not apply; the contracting parties reserve the right to further regulate and subsidize audiovisual production, and agree only on transparency and consultation if GATS members suffer injury.³³ National authorities in broadcasting and films are not restricted by the agreement.

The European Union explicitly considered the Final Act as a success for its position on audiovisual services and is about to use it as a permit for the further intensification of protectionist measures during the five-year period after which further negotiations on liberalization are scheduled.³⁴

European Industrial Policy

The General Directorate X of the European Commission is going to launch a new industrial policy in audiovisual software. At the beginning of 1994, it published a Green Paper entitled "Strategy Options to Strengthen the European Programme Industry in the Context of the Audiovisual Policy of the European Union" and the "Report by the Think Tank", which outline the strategy. It is expected that the Green Paper's recommendations will, after discussion with the member states and the audiovisual industry, be implemented by a Commission decision in 1995. So far, three main fields of industrial policy activities can be identified.

□ The most controversial instrument, television quotas, will be made even more restrictive. Quotas will apply not only to overall transmission time, but also to prime-time programming. Alternatively, quotas might apply to the financial amount of software purchases by each television station dedicated to European productions. Also, quota rules will be imposed more strictly including financial sanctions.³⁵

□ A special levy is being considered, which would be imposed on box office tickets, video cassettes, advertising revenues and broadcasting fees. This levy would be used to subsidize European productions, in addition to national film promotion programmes.³⁶ The Think Tank suggests a complementary fund of ECU 1 billion to assist production.³⁷

□ Special attention will be paid to the European distribution of member states' productions, which nowadays suffer from the fact that the use of most of them is practically confined to the country of production because marketing is inadequate (and because of cultural discount). This includes support for multinational co-productions and pan-European pre-sales, as well as subsidies to cinemas which reserve a specific percentage of their showings for European productions. Another specific fund of ECU 1 billion for the creation of European distribution consortia has been suggested. It is designed for giving low-interest loans to companies with establishments in all member states which distribute European films in all countries of the community.³⁸

The promotion of pan-European marketing and distribution networks as well as multinational co-productions and co-financing is an appropriate method for developing the European production industry, provided that the subsidy portion of the loans is small. The production subsidies financed by a levy on audiovisual revenues is designed as a discriminatory measure against American imports and is a trade barrier.

The aggravation of television quotas is a substantial and economically unacceptable violation of the GATT spirit of free trade in services. It can be predicted to result in new trade conflicts with the United States. It also will not be effective as far as cultural objectives are concerned, nor is it promising for the goal of European audiovisual competitiveness.

³⁰ Cf. Michael Dupagne, *op. cit.*, p. 14.

³¹ Cf. Clint Smith, *op. cit.*, p. 106.

³² This brief outline is based on information from the German Ministry of Economic Affairs. For some details cf. *Financial Times*, December 15, 1993, p. 6.

³³ The German government, for example, assumes that this does not apply to American producers because of their market dominance.

³⁴ Cf. European Commission, *op. cit.*, pp. 38ff.; Think Tank, *op. cit.*, pp. 48ff.

³⁵ Cf. European Commission, *op. cit.*; Think Tank, *op. cit.*, pp. 49.

³⁶ Cf. European Commission, *op. cit.*, p. 61. Inofficial statements mentioned a levy as high as 5% of all respective revenues.

³⁷ Cf. Think Tank, *op. cit.*, p. 57.

³⁸ Cf. Think Tank, *op. cit.*, p. 55.