Why Study State Aid for Film? A Necessary Clarification

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1 State Aid for Film Is a Contested Terrain

> The economics of film determines its infrastructure—its foundations—and therefore its potential. The politics of film determines its structure, that is: the way it relates to the world (James Monaco, 2009, p. 289)
>
> A movie is risky, but if the illusion of control convinces a manager that the risk can be controlled by putting a star in the movie, or adding special effects, or introducing a story line for broader appeal, or spending heavily on advertising, then we will get just the kind of movies we have today. But, the risks cannot be controlled; they are inherent in the very nature of the business (Arthur De Vany, 2004, p. 270)

Ever since governments have first offered financial support to film media, many countries around the world have tended to introduce similar aid programs to support the development, production, distribution, and exhibition of films and audiovisual works in their countries.

In Europe, *State aid for film* has undergone different phases: from establishing automatic film aid mechanisms (1950–1957) to the development of selective film aid schemes (1959–1981), the first wave of regional aid development (1980s) the emergence of broader aid for audiovisual production (1980s), and the search for a

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new balance between cultural and economic objectives as a fifth phase (Lange & Westcott, 2004, p. 17).[1]

Today, the policy practice of handing out film subsidies is ever more challenged. While state authorities continue to subsidize their film as a genuine cultural asset worthy of political protection, they seem to slip into the horns of a fundamental dilemma: On the one side, their schemes represent the vision to strengthen artistic talent and creativity, safeguard cultural diversity, foster cultural integration, and improve the economic wealth of the film industry and its stakeholders at large (European Commission, 2014).[2] On the other side, however, they face a legitimacy crisis as their schemes are perceived as being inefficiently allocated, unfairly distributed, and bureaucratically organized, and, worse so, they are said to help little to adapt to future changes needed to get film media adapt to changing market needs. Not surprisingly, research into film subsidies is no less challenging as subsidies are a controversial means to regulate film media markets and seem to have an in-built bias toward failure in that they:

- May unduly endanger artistic freedom and expression
- Do not correct the fundamental problem of market failure in the industry[3]
- Are considered as economically ineffective as “free markets” work better[4]
- Are a waste of taxpayers’ money as costs exceed benefits to consumers and producers
- Are considered to be politically charged as far as they require consent across opposing political forces backed up by a solid and impartial method of selecting projects and channeling the money to them
- Cannot create long-term sustainability but instead create dependence on the handouts of the state
- Do not improve the working conditions of producers, filmmakers, and other creative staff
- Do neither incentivize consumption of audiences nor improve their satisfaction with the films funded

[1]See also De Vinck (2011).

[2]If one lays aside any definitional problems, “State aid for film,” at a very fundamental level, refers to direct cash grants in aid to filmmakers, film distributors, and cinemas, as well as to indirect tax incentives and rebates to filmmakers.

[3]By contrast, we suggest that “market failure” explanations can go some way in explaining observed regime variety and hence efficacy and certainly take us beyond superficial ideas of the “nanny state” or its converse, but cannot predict a substantial proportion of observed negative effects of film subsidy offerings and its paradoxes. For market failure vs. government failure controversies, see Cowen and Crampton (2002), Dal Bó (2006).

[4]Traditional theorists of the “free-market” school believe in some variation of the “efficient market hypothesis,” essentially a conviction that prices not only reflect all current information but also adjust immediately as new information comes in.

Indeed, as it seems, many schemes need a systematic overhaul. They are perceived as being erratic, contradictory, overworked, and obtuse. What is needed are simpler rules, more transparent application and assessment procedures, clearer selection criteria, more effective instruments, better informed policy, and more direct contact between policy, administration, and beneficiaries.

But slowly, why do these biases between ideation, purposing, and policy transfers exist? Why is it so difficult to support film? Certainly, perhaps because not only are film producers and their industries facing a variety of profound challenges that come to severely threaten their long-established ecosystems, but also are the current challenges to political governance in film economics more prominent than ever before.

2 Understanding Industry Challenges Is Key

Digitization, convergence, intensified competition, and audience fragmentation are all shaping current film media ecosystems, while legacy film producers do not only feel the squeeze of increasing competition for revenues but also see their role as facilitators of cultural expression diminishing. Meanwhile, the financing model of traditional audiovisual media is under pressure as a result of a change in the way in which film is developed, produced, packaged, and distributed, and audiences for online platforms, digital formats, and mobile content are rather dramatically growing (European Commission, 2014; Gubbins, 2012). This is crucial as the promotion of public interest in film as a medium of communication, as an art form and in the development of an informed and critical film audience, is critically endangered. Few observers can imagine public film policies veering off in a wholly new direction, but the pressures of change from outside the schemes mentioned above together with ongoing deficits have forced many governments under study to consider reform.

First if not foremost, one has to question whether public support can mitigate trends of cultural globalization and the dominance of the American film industry: Obviously, as scholars in film industry studies have long pointed out, a discussion of national cultural policies shows that film policy contributes to the success of national film industries but does not enable them to challenge US dominance. Hollywood majors such as *Warner Brothers* and *Walt Disney* have internationalized their businesses through corporate integration (Lee & Jin, 2017; McDonald & Wasko, 2007; Miller, 2016).[5]

Whether by design or not, the global film industry shows healthy projections for the coming years, as the global box office revenue is forecast to increase from about USD38 billion in 2016 to nearly USD50 billion in 2020. The USA is the third

[5]Supposedly, Hollywood's hunger for integration and maximization of global box office receipts has led to changes in the content of Hollywood film toward "deculturized," transnational films, a trend that is also evident in other countries (Crane, 2013).

largest film market in the world in terms of tickets sold per year, only behind China and India (https://www.statista.com/topics/964/film/). Cinema screens increased by 8% worldwide in 2016 to nearly 164,000, due in large part to continued double-digit growth in the Asia Pacific region (+18%). The number of digital screens (+17%) and premium large format screens (+11%) also saw double-digit growth globally. Today, 95% of the world's cinema screens are digital (MPAA, 2016).[6]

It is also well known that there are other organizational reasons for the supremacy of Hollywood cinema worldwide. Miller (2001) identified these in "superior production values, cartel conduct, cultural imperialism manufacturing the transfer of taste rather than technology or investment, and American sign-value as the epicentre of transcendental modernity—fixing social and individual problems via love, sex and commodities" (p. 146). The market power of the Hollywood majors in feature film markets is also well attributed by the argot of scholars of the political economy of the media. For example, Colin Hoskins, McFadyen, and Finn (1997, pp. 61–2) see "a degree of concentration in the feature film distribution industry and (. . .) an economies-of scale barrier to the entry of new competitors" and make a point for the crucial question "whether this structure has remained workably competitive; whether film distribution remains a contestable market."

As it stands, the European film industry, by contrast, is characterized by some unique characteristics: First, the EU is one of the largest film producers in the world. In 2016, its film industry produced 1336 feature films, compared to 817 in the USA, 1255 in India, and 588 in China. However, as Richeri (2016) claims, "the place of the European film industry and market is different because Europe has a lot of problems to deal with: industry and market fragmentation, little cooperation among member states, lacking distribution of European film outside national markets and too large box office share of Hollywood films" (p. 312, *Abstract*).

It is true that the objective of protecting and promoting Europe's cultural diversity through audiovisual works can only be achieved if these works are seen by audiences. Aid to production alone risks stimulating the supply of audiovisual content without ensuring that the resulting audiovisual work is properly distributed and promoted. It is therefore appropriate that aid may cover all aspects of film creation, from story concept to delivery to the audience.

By contrast, American state governments, for the better part of two centuries, have employed targeted tax incentives to promote local economic development. Rising competition, both domestic and foreign, has driven the proliferation of

[6]The global film industry shows healthy projections for the coming years, as the global box office revenue is forecast to increase from about USD38 billion in 2016 to nearly USD50 billion in 2020. The US is the third largest film market in the world in terms of tickets sold per year, only behind China and India (https://www.statista.com/topics/964/film/). By comparison, the EU had 991.4 million admissions in 2016, a gross box office (GBO) of 7,04 billion euros, and 1740 feature films produced; the figures for India are 2.015 million, GBO of USD1.5 billion, and 1.903 films produced; for the USA, 1.195 million admissions, GBO of USD10.280 million, and 789 films produced; and for China, 1.370 million admissions, GBO of USD6.6 billion, and 944 films produced) (European Audiovisual Observatory, 2017a, 2017b).

programs such as enterprise zones, tax increment financing, and hiring incentives (Thom, 2016). Following a 10-month investigation in 2012, the *New York Times* estimated the number of targeted programs at nearly 1900 with an annual cost of over USD80 billion.[7] In the USA, however, the spread of targeted incentives has occurred despite doubts regarding their efficacy.[8]

Still, the European film sector suffers from an apparent disconnection between supply and demand, as the USA is the largest presence in Europe's audiovisual markets. In terms of cinema admissions, US films typically account for 60–65% of the market, versus 25–30% for European films.[9]

The causes for this imbalance are varied and complex, but one major weakness is obvious: the European market for European films is fragmented along linguistic and cultural lines, and the market players are predominantly small to medium sized. While this positively reflects in a culturally diverse output, it represents a significant challenge for access to finance and markets. The audiovisual sector is a high-risk, prototype industry, so the integrated nature of the major US studios and their large domestic market and their much higher production and marketing budgets are very difficult for these small European players to challenge. The linguistic and cultural differences add to this and limit the cross-border circulation of European audiovisual works within Europe even further.

3 State Support to Film in Europe Is Pivotal

In the European film sector, the *European Commission* adopted a new "Communication *on State aid for films and other audiovisual works*" on 16 November 2013.[10] This new "Cinema Communication" provides an updated set of rules for assessing whether European member States' audiovisual support schemes comply with EU rules on State aid.[11] It gives clarity to market players on the criteria that the Commission will apply when examining notifications by member States. On 17 June 2014, the Commission declared certain categories of aid compatible with the internal market in application of Articles 107 (3) (d) and 108 of the Treaty on the Functioning of the European Union.

[7]See http://www.nytimes.com/interactive/2012/12/01/us/government-incentives.html

[8]Tax incentives have also been the target of legal challenges over the Dormant Commerce Clause and claims of taxpayer injury (e.g., *Cuno v. DaimlerChrysler*).

[9]See *European Audiovisual Observatory*. Lumiere Database.

[10]*Communication from the Commission on State aid for films and other audiovisual works*, OJ C 332 of 15 November 2013, p. 1.

[11]*European Audiovisual Observatory* (2014). The new Cinema Communication. IRIS plus 2014–1.

The review of the rules in the Cinema Communication of 2012 was extensive and reflected the important role films and other audiovisual works play in Europe at the crossroads of culture and the economy.[12] On the one hand, European audiovisual production is an important source of creativity and cultural diversity—one that contributes to defining European cultural identity. On the other hand, cinema is an industry, which has a European dimension. Its activities, just like those of other sectors, are embedded in the EU Single Market.

While the EU film sector is dependent on state support—whether at subnational, national, or supranational level.—*State aid for film* is said to be necessary in order to ensure such subsidies are in the common interest and a level playing field between all member States is preserved. Likewise, State aid to promote culture is allowed by the *Treaty on the Functioning of the European Union* (TFEU) through a specific derogation (Article 107(3)(d)). Taking into account the particular nature of the audiovisual sector, the *Commission* established specific criteria in the Cinema Communication for assessing the compatibility of audiovisual support. These criteria aim to achieve a balance among economic, cultural, and legal concerns.[13] By tackling a number of recent sector evolutions and support trends, the new Cinema Communication ensures continued legal certainty, to the advantage of member States, sector professionals, and—ultimately—European audiences.

In all, audiovisual works, particularly films, play an important role in shaping European identities. They reflect the cultural diversity of the different traditions and histories of the States and regions within Europe and abroad. Being hybrid in nature, audiovisual works are both economic goods, offering important opportunities for the creation of wealth and employment, and cultural goods which mirror and shape our societies. Consequently, the film industry is today labeled as a "cultural industry" (Hesmondhalgh, 2005, 2012) and said to belong to the "creative industries" (Caves, 2000; Flew, 2013), a paradigmatic shift that epitomizes that film is to be associated not only with the arts and culture and the social and cultural norms that shape and are shaped by film media but also with economic and institutional structures and hence all issues surrounding the performance of state support.

Still, those who question the value of continued state subsidies to film not only criticize their political ramifications but consider subsidies misappropriated as they slip into filmmakers' pockets with no obvious return. Ending up as backdoor subsidies with no clear benefits, only artificially keeping alive those who are already economically weak, they do little to balance the structural inequalities of the market. As a result of these criticisms, regulators are increasingly shying away from their programs as concerns over the economic efficiency get the upper hand. In

[12] Communication from the Commission on certain legal aspects relating to cinematographic and other audiovisual works, COM/2001/0534 final, OJ C 43 of 16 February 2002, p. 6.

[13] *European Union* (2014). State aid rules for films and other audiovisual works. Competition policy brief. KD-AK-14-013-EN-N, https://doi.org/10.2763/73881

any case, more control is needed so that subsidized film can be persuaded to adjust to more competitive economic environments.

From the policy perspective, State aid(s) to the audiovisual industry are allowed and designed as part of the internal and external policies of the European Union aimed at enforcing the 2005 UNESCO Convention on the Protection and Promotion of the Diversity of Cultural Expressions. The Convention notes that the fact that a film is commercial does not prevent it from being cultural. But being a cultural activity also does not exclude its commercial character. Thus, the State aid rules apply to financial support for the sector.

4 State Aid for Film Is an "Unruly" Research Field

We start exploring key issues that apply to all researchers who seek a generalized and systematic understanding of public support to film. Theoretical focus is on economic theory, policy analysis, and corporate-level strategic positioning of media firms.

However, we first have to concede that the field of *State aid for film* is "unruly" and complex and entrenched by many disciplines such as law, economy, film and media studies, and business administration also. Moreover, the field in itself is complex.

First, subsidies are a notoriously difficult concept to grasp. They only seem to become more tangible when referring to their main purpose: "Subsidies are provided to promote media industries, support political activities, spur cultural development, meet the needs of minority linguistic and ethnic groups, assist religious and other organizations sanctioned by states, and reward political allies" (Picard, 2008, p. 4891).

In Europe, public funding for film includes direct cash subsidies, fiscal incentives, mandatory obligations for broadcasters to invest in film and audiovisual production, and guarantee facilities (i.e., facilitation of access to finance) are the main funding sources. Other funding sources may come from private equity, loan capital, or shareholder equity.

The issues surrounding the management of film funding are, however, far from straightforward, and the underlying economics are highly complex. Frankly, it is difficult to deconstruct these many interrelated phenomena. But it is precisely for that reason that we should not throw down the gauntlet, however. We need more and better research to study the phenomena involved. Truly, we consider intellectual laziness and disinclination to investigate the complex issues involved as myopic and fatal.

In economic theory, films exhibit increasing returns to scale, high fixed and sunk costs, and significant economies of scope. This means that film industries in general tend toward concentration since cost savings achieved by a certain volume of films produced (economies of scale), between different films produced within one company active in more than one market or across more steps of production (economies of scope), or between networks of different suppliers and audiences (economies of networking) lead to a distortion of fair competition with overall welfare losses for the viewing public. This also means that setting prices equal to marginal cost will generally not recoup sufficient revenue to cover the fixed and start-up costs of a film production. And the standard economic recommendation to set prices at marginal cost will fail to cover total costs, thus requiring a subsidy, albeit not necessarily from the public purse (on film financing and “movie economics,” see Chisholm, Fernández-Blanco, Ravid, & Walls, 2015; De Vany, 2004, 2006; La Torre, 2014; Litman, 2000; Moul, 2005; Throsby, 2001, 2010; Vogel, 2014).

Another observation made by economists, sociologists, and other analysts alike is that when the market size increases, so do demand uncertainty and the importance of scale economies. As for most cultural industries, consumer tastes for films are unpredictable, and it is difficult to foresee any film’s success or failure at the box office (for a review of movie economics, see McKenzie, 2012). Thus, market failure seems to be the rule, not the exemption.

That the movie industry is complex and that it operates under high risk and uncertainty are standard inferences for anyone who has been even a casual observer of, or participant in, the process of financing, making, and marketing films (Hjort, 2012). As Vogel (2014) wryly noticed, “seemingly sure-bet, big-budget films with “bankable” stars flop, low-budget titles with no stars sometimes inexplicably catapult to fame, and some releases perform at the box office inversely to what the most experienced professional critics prognosticate” (pp. 144–5). Yet, amid those paradoxes, public subsidies may help refund the start-up costs, get the film production processes going, create and safeguard jobs, and enhance value in any stage of the industry chain. Film production companies, film studios, film production, screenwriting, pre- and post-production, film festivals, distribution, and the “human factor” involved, i.e., actors, film directors, and other film crew personnel, will thus be helped out.

If films are further said to confer properties of merit goods, in the sense that their provision and use benefit society at large as objective information, high culture, and education are promoted, subsidies are well legitimate (Musgrave, 2008).

Economic theory addressed State aid for film (and audiovisual services) mainly from three angles: welfare economics and public finance, cultural and media economics, and cultural and media policy studies (Frey, 2011; Peacock, 1969, 2006; Towse, 2010). In general, economic theory, state subsidies serve two main purposes: (1) they should reduce a person’s or company’s cost of producing and bringing a film to market, (2) and, secondly, by reducing the price of producing and delivering the film, they should increase its consumption beyond what competitive market forces would provide for.

For producers, state aid in the form of a subsidy works like a negative tax as they are given (and not taken) by government and, in the most general case, should encourage the production and consumption of a specific good considered worthy being subsidized. In most cases, subsidies are given out to producers (and distributors and, sometimes, consumers) in order to encourage supply but, occasionally, government can offer a cash or in-kind subsidy to the consumer which itself aims at boosting demand in a market.[14]

Once the product is made, producers use distributors to introduce the movie in the theatrical market. Finally, exhibitors are agents that run theaters and place movies on their screens to attract audiences to generate box office revenue. The distributor is thus the product "ennobler," packager, sometimes also finance provider, and marketing specialist. He markets a motion picture, placing it in theaters and advertising and promoting it.

All of these financial resources may cover for any financial commitment needs (Lacy, 1992), add to the organization's survival based on its optimal utilization of both internal and external resources (Pfeffer & Salancik, 1978), optimally balance these financial resources in order to relieve from financial distress (Modigliani & Miller, 1958), or support the capital structure of the media firm in order to leverage any future investment needs (Myers, 2000).

Clearly, films are not economic goods only but also cultural goods which mirror and shape our societies. "Arthouse films," which are typically independent films aimed at a niche market interested mainly in film arts, for example, confer properties of "pure" cultural goods in the sense that their provision and use benefit society at large. The protection of these films has developed in an interplay with the state, which has shouldered its responsibility to safeguard and promote the public service function of film. This higher-level goal may be preserved by government (Frey, 2011).

Film funding, by itself, is involved in all phases of a film's production, from planning and writing and development of the screenplay to production itself including all forms of distribution, mainly theatrical exploitation. Furthermore, a number of measures such as consulting, public relations, awards, etc. are subsidized. Hence, film subsidies follow a public policy purpose in culture which is essential for pluralism (including geographical, linguistic, cultural, and political pluralism) in an open society. Indeed, film matters: It affects us in our daily lives and is full of meanings that are valuable to all of us. And beyond, a mature democracy should have the courage and the understanding to see the "debt" it owes its artists and to continue to support them, because what it gets in return—economically, socially, aesthetically—is greater than that which it dispenses, not only in terms of production of cultural reflection and identity but also in terms of safeguarding a pluralistic discourse beyond information and classical journalism.

[14]Ross argued that to rise welfare of an individual at the lowest possible cost, cash grants are more efficient than subsidies to the consumption of specific commodities (Ross, 1988). Equally, Peltzman (1973) looked into education subsidies and found that an in-kind subsidy, such as below-cost education provided by state universities, replaces more private consumption of the subsidized good than an equivalent money subsidy, such as a scholarship.

5 "Good" Governance Is Difficult

If we affirm that independence and pluralism in the media are in fact preconditions for democracy to flourish, it is still possible for key elements in government to be committed to media that do not unduly interfere with decisions made by individuals, groups, or media firms regarding social and economic matters. The question how this pluralistic film landscape can be ensured by governmental frameworks is in the center of the debate on the boundaries and possibilities of governance. As laissez-faire under the preconditions of market failure and globalization would lead to a dominance of mainstream film products (and certain regions of production), direct intervention is against the democratic constitutional rules of freedom of art (and expression). However, a positive relationship between the state and media goes beyond pure laissez-faire to nourishing an independent and pluralistic film media landscape. Obviously, a system of "good" governance, in a very general sense, is needed that goes beyond restrictive legal governance and control, but instead is brought to bear on effective techniques or means that film policymakers may use in their attempts to achieve policy goals in the public interest.

This is, of course, a difficult process in that it seeks to implement a system that is both well-targeted, unifying, and boundary-spanning and emphasizes that administration interacts with their environments such that its design, organizational principles, and control parameters are efficient and effective at the same time (Jordan & Turnpenny, 2015; Price, Puppis, & Verhulst, 2013; Rosanvallon, 2016).

As mentioned, the rationale behind the financial supports to cultural sectors such as film is that the culture is a key tool to promote the European single market and to foster social integration through the respect of cultural diversity. In fact, the so-called cultural exception allows member States to grant support to the industry in accordance with the commitment of not distorting competition.

Theoretically, discussions about market failure reflect disputes among scholars of different schools of economic thought, notably between doctrinaire positions of the "free-market school" versus the market-interventionist axis of scholarly reasoning. As it stands, the academic debate about the paradigm of market failure is complex and rather confusing. It originates from the paradigm's hybrid intellectual architecture and results in competing scholarly discourses. Here, two dominant schools fight for scholarly hegemony: On the one hand, the Harvard-MIT-axis of scholarly reasoning in economic theory argues that in case of market failure, government is to intervene in the economy to correct for those and to restore the conditions for welfare optimization (Musgrave, 1959; Musgrave & Peacock, 1958; Samuelson, 1954).[15] Counterarguments on that way of thinking come from the neoclassical '*Chicago school*' of economic thought (Stigler, 1988).[16] Their

[15]Paul Samuelson (1954) and Richard Musgrave (1959) and others consolidated the market failure paradigm in the 1950s. However, this paradigm was contested since its inception.

[16]The term was coined in the 1950s to refer to economists teaching in the Economics Department at the University of Chicago, such as Frank Knight, Ronald Coase, and Milton Friedman.

fundamental tenet is that competition within a perfect market will lead to efficiency, which is the desirable normative goal of the legal system. According to the Chicago analysis, intervention within the market is justified only when there is a market failure. For them, such failure exists when there are no multiple players on both sides of the market (the problem of monopoly), when these players do not have symmetric and full information relevant to their market activities, when any of the players bypass the market through involuntary actions or when the traded commodity is a public good. The general orientation of the *Chicago school of economics*, however, is that these circumstances are rare and that in the real world there is too much central intervention (Reder, 1982). Media markets would thus have strong tendencies toward failure. Now, these are opposing schools of thought. But is their explanatory power still strong enough today? The *paradigm of market failure* is a doctrine within economics which explains the notion that self-regulated markets reveal structural and behavioral instances that lead to their failure in working efficiently as a result of which corrective government action seems warranted (Bator, 1958; Cowen & Crampton, 2002).[17] Traditions in the *political economy of the media*, by contrast, look into the issue of government control over the media whereby government may seize the media and induce bias such that film would manipulate opinion in favor of government interests. The government may have vested propaganda interests in fostering the film industry: it may want people to see films that will inculcate the values of government. And it may want to spread a more attractive image of the country abroad (Gehlbach & Sonin, 2014; Prat & Strömberg, 2011). In this respect, European and national public funds are intended primarily for small companies—mainly of the cinema sector—with low market share and independent from broadcasters and thus focus in general in the compensation of market failure and to ensure political goals such as regional production, image transfer, and the stimulation of cultural production and quality. The broad scope of media cultures and media systems is also reflected in state aid systems for the film industries.

5.1 Sources of Funding

State aids for film are refunded by supranational, national, federal, and local government budgets, levies, and taxes but also from lottery proceeds. Films productions and other forms of cinematographic expression are, of course, sourced from sales revenues made at the box office, cinema advertising revenues, private investments in production, and sponsoring activities of any kind. Naturally, private

[17] Arthur Cecil Pigou has been called the father of the market failure paradigm. Indeed, he argued that “in any industry, where there is reason to believe that the free play of self-interest will cause an amount of resources to be invested different from the amount that is required in the best interests of the national dividend, there is a prima facie case for public intervention” (1932, p. 331). He suggested that taxes could be used when external diseconomies are present and that the existence of external economies would warrant the use of subsidies.

financing sources from industry, including in-house financing and production-finance-distribution deals with TV companies, TV pre-sales, debt financing, and end-user financing play another key role in refunding film projects. The key issue in this regard is access to these financing sources.

5.2 Institutional Framework

Film subsidies are provided within certain legal and institutional frameworks that are shaped by societal expectations to film media subsidies and (political) regulation (De Vinck, 2011).

The legal basis is particularly significant in this situation. Laws have been enacted on the European level (EU State aid law), and they focus on the aspect of protecting competition. In addition, there are national and regional media-subsidization laws for the specific sectors. Other media-subsidization laws on the national and regional level apply to the specific media sectors. They too must comply with the European Union's State aid law and must conform to the legal principles that touch upon media subsidization (freedom of the press, freedom of competition, equal rights, and guarantee of property rights). In addition to classic forms of media regulation such as media-business law (e.g., media-antitrust and media-competition law, merger control, etc.), there are areas of media subsidization with their own regulations: press, broadcasting, film, and business subsidies and subsidies for political parties. Thus, media-subsidization laws can be found in a number of different legal fields.

5.3 Subsidy Types

Media policies have been designed in many European countries to promote media pluralism and diversity. Negative rules on curbing media and cross-media ownership aim at setting limits on media concentration, whereas positive rules such as different forms of direct or indirect public sector support aim at maintaining a healthy and prolific media industry. Along with the interrelationship between different localities and specific historical, cultural, and political perspectives, policy regimes, and technologies/media, however, different countries have developed different film policy regimes. Hence, it comes as a natural feature that the development of film media is not only exclusively based on economic principles but also on sociocultural, political, and democratic frames to preserve the public interest (Bondebjerg, Novrup Redvall, & Higson, 2015).

First, there are different types of support for film policymakers to support the financing of film and audiovisual production (Fontaine, 2015; Talavera Milla, Kanzler, & Fontaine, 2016):

- Direct public support through film funds (covering a wide array of automatic and selective aids to the film and audiovisual industries, covering all stages of the value chain (development, production, distribution and marketing, exploitation), as well as aid to technical industries and research and development)[18]

- Fiscal incentive schemes (e.g., tax credits for production, distribution, exemption from business tax, special VAT rules, special amortization and depreciation rules, measures aimed at investors)
- Investment obligations into film of TV broadcasters and other stakeholders[19]
- Guarantee facilities (facilitation of access to finance, loans guarantees)

On a pan-European level, funding levels have remained fairly stable over the past years, and the fiscal incentive schemes are being used as complementary instruments to support the film and audiovisual sectors. Importantly, contributions from the national/federal government and broadcasting levies were the two main sources of financing for film and audiovisual funds in Europe. Contributions from the administration at all geographical levels have hardly compensated for the steady decline of income from levies on broadcasters. MEDIA, the European Union's support program for the film, television, and new media industries, for example, offers a variety of funding schemes, each targeting different areas of the audiovisual sector, including schemes for producers, distributors, sales agents, organizers of training courses, operators in new digital technologies, operators of video-on-demand (VoD) platforms, and exhibitors and organizers of festivals, markets, and promotional events. It encourages the circulation and promotion of European films with particular emphasis on non-national European films. These actions were continued in the MEDIA subprogram within *Creative Europe*, the new European support program for the cultural and creative sectors. Regarding the scope of aided activities, some States offer aid to activities other than film production. This includes aid to film distribution or to cinemas, for example, to support rural cinemas or "arthouse" cinemas in general or to cover their renovation and modernization, including their transition to digital projection. Other States support audiovisual projects which go beyond the traditional concept of film and TV productions, in particular interactive multimedia products such as transmedia or video games.

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[18]Steenblik stressed the importance of direct subsidies but noted that other, indirect subsidies would also play an important role as they would bring regulatory relief to suffering industries: "Many subsidies are indeed provided in that form, as grants or, more generically, direct payments. Grants are the elephants in the subsidy zoo: they are large and highly visible. But there are numerous other subsidy beasts which are better camouflaged, stealthier, and keep closer to the ground" (Steenblik, 1990). Any of these kinds of financial transfers aim at (re)funding the operational activities of companies the market does not efficiently allocate for and, importantly, governments and other stakeholders would have an interest in to be supported.

[19]Rather little is still known about these "mandatory investments" for film. These are compulsory interbranch financial transfers. Organized by public authorities through binding legal agreements, they can take the form of (a) an implementation of a specific tax or levy to finance a national film fund or (b) a legal definition of mandatory investments into film production.

5.4 The Politics of Subsidy

If state aid is politically approved—and policy history and market imperfections are not, in themselves, a sufficient condition for concluding that financial support is warranted—regulators face the obvious choice of publicly financed subsidy approaches, either through direct cash injections, indirect cash advantages, anti-trust policies as means of regulatory state action, or, most likely, a combination of these. When society's goal is to raise the welfare of an individual, household, organization, industry, or society at large, regulatory action may be taken by a government in order to affect or interfere with decisions made by individuals, groups, or organizations regarding social and economic matters.[20] Financial subsidies to film, on their part, typically seek to balance the objective of promoting economic competitiveness in the media grid with the wider objective of securing cultural diversity and wider social benefits. Supportive governments then need to organize that the range of films on offer should be broad, varied, and of high quality. The public should have access to films regardless of where they live and irrespective of what platform they want to use. Public film policy via subsidies should support both ambitious and artistic filmmaking as well as foster their commercial opportunities. It would be in the society's best interest if public subsidies strengthened diversity in media and opinion, motivating the production of high-quality content, and supporting its delivery and consumption and across borders and ideologies. Two basic schools of thought have emerged on regulatory policy, namely, *positive theories of regulation* and *normative theories of regulation* (Frey, 2011). Positive theories of regulation examine why regulation occurs. These theories of regulation include theories of market power, interest group theories that describe stakeholders' interests in regulation, and theories of government opportunism that describe why restrictions on government discretion may be necessary for the sector to provide efficient services for customers. In general, the conclusions of these theories are that regulation occurs because (1) the government is interested in overcoming information asymmetries with the operator and in aligning the operator's interest with the government's interest, (2) customers desire protection from market power when competition is non-existent or ineffective, (3) operators desire protection from rivals, or (4) operators desire protection from government opportunism.

Normative theories of regulation generally conclude that regulators should encourage competition where feasible, minimize the costs of information asymmetries by obtaining information and providing operators with incentives to improve their performance, provide for price structures that improve economic efficiency, and establish regulatory processes that provide for regulation under the

[20]In economic theory, the first fundamental theorem of welfare economics describes an idealized system of equilibrium conditions to efficiently coordinate economic activity (Pareto, 1971/1927). Markets that do not achieve this Pareto-optimality are said to result in market failure.

law and independence, transparency, predictability, legitimacy, and credibility for the regulatory system (See footnote 8).

5.5 Policy Designs and Objectives

When it comes to policy design, effective governance plans for supporting a whole industry will first have to identify the big picture when aiming to resolve an ailing or otherwise to be supported industry, all the way from setting clear and realistic objectives to measuring subsidy-impacted industry performance and output. Naturally, effectively designing these schemes is a very difficult task (Jordan & Turnpenny, 2015). While it is notoriously difficult to strike this balance in an ever-changing and highly dynamic media environment, policymakers may need to conciliate between the following motives—among others—behind public film policy and the subsidy rationale that emanates from them (Baldwin, Cave, & Lodge, 2010):

- Curbing the market power of dominant firms (e.g., by handing over subsidies to "weaker" newspapers)
- Enabling market access for new entrants (e.g., of nonprofit or not-for-profit organizations)
- Relieving financial distress to keep companies alive
- Supporting market exit (e.g., of failing companies)
- Supporting a political purpose (which need not be in the public interest)
- Supporting a national/regional/local culture and its linguistic representations
- Enabling growth and innovation plans of a media company
- Improving journalistic quality for general public benefit
- Encouraging political discourse and the formation of public opinion
- Protecting vulnerable values and groups in society (e.g., linguistic plurality and ethnic diversity)
- Strengthening of the national industry and offering incentives for newspapers not to relocate
- Safeguarding political plausibility and civic support

5.6 Subsidy Effects

Clearly, evidencing the *economic impact* of film subsidies has recently become a first-order rationale for governance and state intervention, if not their raison d'etre in times when film culture is considered as belonging to the "creative industries" (*Hesmondhalgh,* 2012).

Although creating benefits from subsidies to culture is far from being a new academic proposition (Heilbrun & Gray, 2001; Throsby, 2001; Towse, 2010), the effects debate warrants much closer study from the perspective of media policy and governance research.[21] Why should government subsidize film? What are the effects of these subsidies? And is a focus on narrow economic benefits of subsidies to film sufficient? Does it not need bigger picture that includes the effects of culture as well? Certainly, effective governance plans for supporting a whole industry will first have to identify the key drivers when aiming to resolve an ailing or otherwise to be supported industry, all the way from setting clear and realistic objectives to measuring subsidy-impacted industry performance and output.

Still, in Europe, film and cinema is conceived more as an art form than as a business. And this is why we believe that one-sided arguments exclusively employing economic effects ignore an extremely important area: film production has cultural value, and the wider effects to culture and society effects *must* be considered equally when evaluating the overall effects of subsidies to film and film production.[22]

Hence, the economic effect, which can easily be counted and quantified, has become a sole yardstick for legitimizing state aid for film to the industry. However, is evidencing film subsidies on purely economic reasons sufficient for legitimating film funding as such? Publicly funded film is under more pressure than ever to quantify the social benefits it brings, as would be done for schools and hospitals. But isn't the crucial role of art to challenge the way society is run? Again, we wish to stress that when film funding seeks legitimation for its action and yardsticks for the success of its work, an integral approach revealing both economic *and* cultural impacts is much more useful. This involves tools for informing, monitoring, and controlling subsidy effects on each side of the equation, hence the design of an "evaluation toolkit" for State aid for film. To our knowledge, such a unifying toolkit does as yet not exist.[23]

6 The Purpose of This Book

This book presents interesting puzzles and illustrates the many problems of public funding for film such as industry change, digital transformation, regionalism, cultural diversity, the "Hollywood factor," alternative models of film funding, gender equality in film production, shifting audience tastes and consumption behaviors, governance efficiency, and more. Based on insights from fields such as cultural economics and studies in public film policy, the authors illustrate how technology and industry change shape both the financial fitness of film and how public film funding can promote both cultural diversity and economic efficiency of

[21]Surprisingly, however, the practice of public subsidies for cultural activity is said to lack a rigorous and consistent economic rationale (Aubert, Bardhan, & Dayton-Johnson, 2001).

[22]On top of this, a purely economic position also ignores the fact that intra-sectoral competition for subsidies among the creative industries has intensified. Who will receive the funds which become increasingly scarce? Theaters, opera houses, museums—or film?

[23]Some attempts are visible: Kumb, Kunz, and Siegert (2016), Kumb (2014).

national and international film industries. It shall help both scholars and practitioners in the film industry to understand the complexity of issues and the requirements necessary to preserve the social benefits of public funding schemes for film.

Arguably, current policy support schemes to film media seem particularly challenging, intrigued by positive, negative, and ambiguous effects on all stakeholders involved. This is not only because European media policy consists of a complex maze of stakeholders, regulatory instruments, and diverging interests (Donders, Loisen, & Pauwels, 2014). As described above, this is due to the fact that the art~~s~~ and culture of filmmaking is presently facing a plethora of profound, if not disruptive, challenges that seriously threaten their long-established ecosystems and so the industry's continued financial viability and competitiveness (European Commission, 2012). Certainly, the "screen art industry" has always been powered by the capabilities of currently available technologies. Be it about the invention of the color television, the progress of cinema-related technology, special effects capabilities, and now virtual reality powered video/movie experiences—the adoption of new technology is clearly impacting the way movies are produced and consumed and other video-related entertainment products.[24] But, would we know how film media will look like in a few years from now, driven by radical technology innovation, increasing audience fickleness, and new financing models shaping industry architectures and business models used within this converged media ecosystem, under the impact of globalization, with China being the "new Hollywood" in filmmaking? (Bao & Toivonen, 2015; Peng, 2015; Richeri, 2016). It is clear that these disruptive potentials, arising from technological convergence, digital transformation, industrial globalization, and audience fragmentation, evoke a nexus of research dimensions. These encompass issues of technological change and innovation; effects of the convergence on filmmaking, distribution, and exhibition; effects on the industry structure and the competitive behavior of market players and their new rivals from outside the industry; the ever-more-important changes in audience behavior; and the creation of public policies to protect consumers and promote high-quality productions.

State aid for film wishes to amplify the discussion on public subsidies for film from various international perspectives. Given the different methods in theorizing, development, realization, monitoring, impact measurement, and evaluation of policy concepts, programs, institutions, instruments, and impacts, this debate is not only of interest for academics but also for policymakers in the field. While creating artistic, cultural, and socioeconomic value from subsidizing film media is far from being a new academic proposition (Lange & Westcott, 2004; Newman-Baudais, 2011; Nielsen & Linnebank, 2011), *State aid for film* offers a much closer study from the range of new perspectives. These include:

[24] Arguably, "Hollywood as we know it is already over," "with theater attendance at a two-decade low and profits dwindling" (*Vanity Fair*, 2017).

- Understanding the changing role of film subsidies as an important policy tool vis-à-vis the market entry of new players from outside the traditional film media industries are increasingly "colonizing" the location in which contemporary identity, culture, and core values and norms are contested
- Exploring how media convergence, globalization, and consumers turning away from legacy channels are major drivers of industry change as new digital distributors of film have emerged, crossing national borders, making media policy in the information society increasingly a transnational concern
- Investigating the quantity and quality of public support for film media as prerequisites for cultural diversity, European integration, and economic sustainability in times of growing media concentration, technological disruption, and political polarization
- Innovating academic discourses on film policy in making them more pluralistic, improving the quality of policy designs, strengthening the validity of evaluation mechanisms, and thus increasing outcome efficacy and their fitness to reach their objectives
- Evidencing the effects of film subsidies on various levels: the industry, the film producers, the creative staff, etc.
- Evaluating the efficacy and existing funding instruments and tools offered, the governance processes and their political framing, and the outcomes and effects of these schemes' efficacy on culture, the society, and the economy
- Analyzing potential biases between purposing, policy transfers, and controlling of these schemes and the challenges to "good" governance and policy quality arising from them

To conclude, the book provides a comprehensive analysis of today's global challenges in the public governance of film funding and hence stresses the necessity of *State aid for film* as an important tool for strengthening media diversity as it stresses film as both a cultural *and* an economic good in a modern democracy.

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