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THE BLOCK-BOOKING OF FILMS: A RE-EXAMINATION

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ABSTRACT: Block-booking, twice banned by the U.S. Supreme Court, involves selling motion pictures as a package. The most generally accepted explanation, developed by Kenney and Klein (1983), is that block booking prevented exhibitors from “oversearching;” i.e, from rejecting films demonstrated ex post to be of below-average quality from a package priced at ex ante average value. This paper examines the way in which the practice developed, the nature of the optimization problem between producer and exhibitor, and the specifics of block-booking contracts, and finds little to support the Kenney and Klein hypothesis. First, block booking emerged at a time when films were very homogenous and no new information about film quality was revealed between booking and exhibition. Second, block booking was applied more flexibly than a primary concern with oversearching would suggest (the flexibility is understandable when one considers that films were sold on a revenue-sharing basis). Third, exhibitors failed to make use of contractually-permitted opportunities to behave in ways block booking was posited necessary to avoid. This paper proposes that block booking was primarily intended to provide in quantity a product needed in quantity, a claim made by the movie producers of the time.

I. INTRODUCTION

Block booking is the selling of motion pictures as a group, or “block.” On two occasions, the U.S. Supreme Court ruled it illegal: *United States versus Paramount Pictures, Inc.* (1948) and *United States versus Loew’s, Inc.* (1962).¹ Scholars have debated why movie producers booked films in blocks. The producers claimed that it merely allowed them to provide in quantity a product needed

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¹ *United States v. Paramount Pictures, Inc.*, 334 U.S. (1948) and *United States v. Loew’s, Inc.*, 371 U.S. (1962). The Paramount case dealt with contracts between film makers and film exhibitors, while Loew’s involved the sale of old films to television stations.

in quantity.² The Supreme Court disagreed, and banned the practice on the grounds that it was used to force exhibitors the purchase films they did not want in return for receiving those they did. Stigler (1963) pointed out the illogic of the Supreme Court's argument, and proposed that block booking was a form of price discrimination, akin to other tying arrangements. Kenney and Klein (1983) rejected Stigler's explanation, and suggested instead that block booking was intended to resolve an oversearching problem, brought about by the fact that new information about film quality (in the form of early box office receipts) was revealed between the signing of the contract and the time when the exhibitor actually received and had to pay for the film. The Kenney and Klein explanation remains the most generally accepted among economists today.

A review of the actual details of movie contracts sheds new light on the debate. At the time of the *Paramount* decision, major films were rented to major theaters on a revenue sharing basis. As a result, both producer and exhibitor gained when a film's run length could be adjusted in line with viewer demand. In the movie business, the demand for a particular film is not revealed until it is actually exhibited.³ Therefore, it would appear optimal to interpret *ex ante* (i.e., before demand is revealed) film exhibition obligations *flexibly ex post* (i.e., after demand had been revealed). But central to the Kenney and Klein hypothesis (as well as to the Supreme Court and Stigler explanations) is the assumption that block booking contracts had to be—and were—*rigidly* enforced *ex post*. Block booking could simply not do what each suggest unless post-contractual adjustments in exhibitor obligations were limited significantly.⁴

² See the arguments made by made by the various defendant producers in the *Paramount* case, such as Loew's (76), Paramount (107), RKO (134), Columbia (155), Universal (174), Warner Brothers (213) and 20th Century Fox (234), as well as the discussion in section II.B.

³ See De Vany and Eckert (1991, 55). See also De Vany and Walls (1996, 1997) for a more detailed examination of the optimization problem facing by film producers and exhibitors.

⁴ Although Kenney and Klein discuss the role of revenue-sharing (524-27), they do not explore its implications for block booking, focusing instead on its effect on each party's incentive to provide such complementary inputs as clean theaters (exhibitors) and high quality films (producers). Contingent pricing, they conclude, economized on brand name capital, and so was used instead of flat fees. By focusing exclusively on the margins for cheating, Kenney and Klein overlook the fact that contingent pricing also aligns producer and exhibitor incentives as to *which* films should be shown, and for how long.

After investigating the history of the package selling of motion pictures and the way in which block contracts were applied, I come to the conclusion that movie producers were correct and block booking was simply intended to provide in quantity a product needed in quantity. Exhibitors required a large number of films to fill their screens (200 or more per year), and wanted a sure and steady supply. At the same time, producers were able to reduce direct selling costs by contracting for films in volume. Thus, films were sold as a package, with the size of the package depending on the exhibitor's needs. Selling in quantity is relatively common in retailer-wholesaler relationships;⁵ what is somewhat unique to the film industry is revenue sharing, which generates different incentives ex post than are typically found.

I begin by reviewing the Kenney and Klein and quantity selling hypotheses in more detail. I follow with an examination of the history of the bundling of motion pictures. I find that package selling emerged in the early days of the silent cinema, when films were so homogenous that they were sold by the foot. The homogenous nature of those films, coupled with the fact that no new information was revealed between contracting and release, is consistent with the producer's explanation for block booking, but not with the Kenney and Klein hypothesis (nor with the Supreme Court's nor Stigler's, for that matter). I then turn to the optimization problem facing movie producers and exhibitors once films became heterogenous in quality (i.e, with the arrival of the feature film circa 1912), and find that ex post adjustments in exhibition obligations—specifically, the extension of popular showings and the abbreviation (or even cancellation) of unpopular ones—were common, although they are precisely what the Kenney and Klein hypothesis posits block booking was intended to prevent. Furthermore, exhibitors appear not to have taken full advantage of *contractually-permitted* opportunities to redistribute revenue from producers to themselves ex post, although the Kenney and Klein hypothesis presumes that only (or at least primarily) the terms of the block contract deterred them from doing so. I also briefly review how film distribution was affected by the ultimate banning of the practice, and the

⁵ Retailers typically sign annual contracts with suppliers that specify various amounts for monthly delivery (the retailer can wait and submit individual orders as needed if it prefers, but, not surprisingly, the price paid per unit is higher). The uncertain nature of movie demand makes it comparable to the fashion clothing business: once fashion sellers are able to observe which lines sell and which do

nature of movie distribution today. In each case, the evidence suggests that the primary objective of block booking was simply to provide in quantity a product needed in quantity.

This is not the first article to propose that block booking was simply an efficient means of selling in quantity.⁶ However, it is the first to tie systematically that hypothesis to an investigation of the history of package selling in the movie business, and to the way in which block booking contracts worked. While the Kenney and Klein argument may explain package selling arrangements in other settings, it does not appear to be the primary reason that films were booked in blocks.

II. EXPLANATIONS FOR BLOCK BOOKING

A. Block Booking to Prevent Oversearching

Kenney and Klein develop their hypothesis in a discussion of how the De Beers Company sells diamonds. De Beers offers diamonds as a package, and only as a package, priced at the average value of the diamonds therein.⁷ Buyers are allowed to inspect the package before buying it, but those who reject a package are never invited back. Kenney and Klein suggest that the De Beers system serves to (1) avoid oversearching by buyers (which would require De Beers to spend more money sorting diamonds), while (2) preventing De Beers from cheating on the quality classification (by allowing customers the right to inspect and reject any given package). By transacting in this way, De Beers and its customers are able to reduce sorting costs substantially, and to share the savings that result.

Kenney and Klein then apply this model to the booking of films. Their essential point is that while it is in the ex ante interest of both exhibitors and producers to minimize sorting, the incentives

not, they adjust price and quantity accordingly—see Lazear (1986) and Pashigian (1988) for models of price adjustment, and Urban (1998) for a model of shelf-space allocation.

⁶ See also Cassady (1959, 382) and De Vany and Eckert (1991, 83-4). Cassady writes, “block booking developed out of the need of distributors for a more efficient method of selling films.”

⁷ All except the largest stones, which are sold on an individual basis for a negotiated price.

differ ex post. The blind selling of films saved on inventory costs,⁸ but raised the possibility of opportunistic ex post search by exhibitors, given that box office receipts from earlier showings were available before films were actually received and paid for (exhibitors could potentially reject those films revealed by audience response to be “over-priced”).⁹ Block booking, by requiring that all films contracted for ex ante be exhibited (or at least paid for) ex post, resolved that problem. The author’s write,

Block booking was used *solely* [emphasis added] as a way to prevent exhibitors from engaging in this post-contractual rejection of overpriced films. . . . Block-booking, or the intentional over-pricing of ex post unexpectedly poor quality films, can be thought of in this context as a means of enforcing blindness, effectively preventing exhibitors from searching out and rejecting the poorest-quality films after first-run results become available. (522-3)¹⁰

As evidence of the severity with which block contracts were enforced, Kenney and Klein cite the liquidated damages clause that took effect if an exhibitor rejected a film from the contracted block (523).¹¹ They also note that such things as run designation could be used to discipline exhibitors.¹²

B. Block Booking as Quantity Selling

In their 1928 testimony before the Federal Trade Commission, producers based their defense of block-booking on the following: (1) it was wholesaling applied to motion pictures, (2) it reduced the cost of distributing motion pictures, and (3) it simplified the buying problem by allowing

⁸ The alternative to agreeing to blocks of films that had not been completed was to keep a season’s worth of films (or part thereof) in a vault until exhibitors were ready to buy (see Kenney and Klein 1983, 521).

⁹ Exhibitors were then organized by “runs,” with first-run theaters showing films several weeks-to-several months before everyone else. See section III below for more detail.

¹⁰ For films sold on a revenue sharing basis, the threat was not actually that “over-priced” films would be rejected (“over-priced” is hard to understand in the context of revenue sharing), but rather that films would be “overbought;” i.e., that more would be booked ex ante than could be shown ex post, with the worst (as indicated by box office receipts) subsequently rejected.

¹¹ In fact, as I will show below, that penalty only applied to films canceled above and beyond a permitted amount—the existence of cancellation clauses, allowing a number of penalty-free cancellations from the block, was not recognized by Kenney and Klein. Penalty-free cancellations were also granted for a variety of other reasons—see section IV below.

¹² See their footnote 70. Of course, the existence of this retaliatory mechanism raises questions as to why a rigid enforcement of blocks was necessary to overcome the oversearching problem in the first place.

exhibitors to obtain a year's supply of pictures in one large purchase.¹³ In short, block booking provided exhibitors with an assured and steady supply of the product while enabling producers to lower direct selling costs. Lewis (1933, 7) writes of early package selling in the film industry: "What the distributors sold and what the exhibitors wanted was a *service*, that is, a constant supply of two or three reels of motion picture film furnished two or three or more times a week."¹⁴ Film journalist A.D. Murphy (1992) writes, "[T]hen [circa 1920] and now, a theater owner would go berserk not knowing what [new] film to put on the screen when a film showing had ended its run." An exhibitor trade association noted in 1938, "The exhibitor is in the position of buying a sufficient quantity of quality product for his theater to insure a continuous supply of merchantable pictures. To quit block-booking would be to greatly increase the price of pictures."¹⁵ In 1923, Famous Players-Lasky, the production arm of Paramount, experimented with replacing block booking by the individual selling of films. It discovered that the new approach upped the number of sales calls from three-to-four to thirty-to-forty per exhibitor per year (one for every two or three pictures). To maintain individual selling, the company estimated that its sales force would have to be quadrupled, sales and overhead costs doubled, and price per picture raised by 40 percent. It instead abandoned the practice.¹⁶

¹³ See Lewis (1933, 148).

¹⁴ A theater following a "one change" policy (i.e., changing programs one time per week), would show films for a week and thus needed approximately 50 films per year if it showed single films and 100 if it showed double features. More common was a two or a three change policy, which meant that the theater showed a film for two to four days, and thus required 150-250 films per year.

¹⁵ Ricketson (1938, 30). An industry spokesman appearing before the Supreme Court testified, "I can sell 40 pictures at \$10 apiece if I can sell him 40. By selling one at a time (or selling a number of smaller groups) I can not sell him at \$400. He could buy the whole package at \$400, throw half the films away, and be better off than if he'd had to buy them individually." See Chambers (1941, 400).

¹⁶ See Lewis (1933, 153). Not all film producers sold their films in blocks. A prominent exception was United Artists (UA), who did not actually produce films, but rather distributed the films of various independent but affiliated producers. Kenney and Klein (527) attribute UA's eschewing of block-booking to its need for accurate measures of individual film values, so as to provide each producer with the return corresponding to that producer's films. Of course, UA could have sold the films of *each producer* in blocks (e.g. a Charlie Chaplin block or Mary Pickford block); indeed, the early "star" blocks were exactly that (see the next section). However, each individual UA producer made only three or four films per year, and the savings in direct selling costs that would have resulted from block selling were correspondingly tiny. This is consistent with the fact that small film production companies generally tended to sell their films individually, despite the fact that they had no need to allocate film revenue between separate entities.

C. Testable Implications

Kenney and Klein recognize that block booking was desirable for the reasons put forward by movie producers, but focus on the rigid application of the block, which they suggest was necessary to resolve the oversearching problem. They thus posit that ex ante block booking contracts had to be enforced rigidly ex post (to a fair degree at least) to prevent that problem from arising. The oversearching problem occurred because films were of heterogenous quality, and because new information about film quality was revealed between contracting and payment. Therefore, in what follows, I will investigate (1) the nature (homogenous versus heterogenous) of packaged motion pictures and of ex post information revelation, (2) the flexibility with which block contracts were applied, and (3) the degree to which contractual terms appear to have been a key factor in deterring ex post exhibitor opportunism. If I find over the history of motion picture package selling that, (1) films were heterogenous and new information about film quality was revealed after contracting but before payment, (2) block contracts were enforced with a fair degree of severity, and (3) exhibitors acted opportunistically to the degree permitted by the written terms of the contract, the Kenney and Klein hypothesis is supported. If I find the reverse, the producer defense becomes the more plausible explanation.

III. A HISTORY OF THE BLOCK BOOKING OF FILMS

The first full-time movie theaters emerged at the turn of the century, and were called “nickelodeons” for their practice of charging five cents admission.¹⁷ Nickelodeons were typically small and uncomfortable, and were located in old dance halls or large shops (not until the late teens would theaters specially constructed for the showing of movies become common). The early “movies” that the nickelodeons showed were very different from what we see today, or even from what a viewer would see one decade later. First, films were quite brief, typically lasting only a few minutes,¹⁸ and

¹⁷ See Merritt (1985) and Allen (1985) for discussions of the nickelodeon.

¹⁸ When the fictional feature *The Great Train Robbery* was released in 1903, it astounded audiences by lasting a full fifteen minutes.

most were documentaries or scenes of landscapes and passing trains.¹⁹ They were typically the product of a single cameraman, who would choose the subject, provide the necessary staging, and edit the result. Advance planning was minimal and no scripts were used, so film “quality,” as we would now judge it, was very low. This was less important than one might imagine; both quality and subject matter came a distant second to the novelty of seeing places and people in motion.²⁰ The relative unimportance of the individual film is revealed by the prevalent pricing practice—films were sold by the foot, and nickelodeons purchased the number of feet they required to make up a show.²¹

The principal problem facing nickelodeons was obtaining an adequate supply of films. In order to operate successfully, a nickelodeon had to present three-to-five pictures per program, and to change programs frequently.²² Few could justify purchasing all the films they required, and instead began to trade films among themselves as local audiences tired of them. The practice was formalized, and a number of film “exchanges” were organized, the first in San Francisco in 1903.²³ The exchanges, typically owned by the exhibitors they served, purchased movies from producers and leased them to exhibitors for about one-fifth the purchase price.

It was at this time and in this context that the first block selling arrangement emerged—the “program system.”²⁴ Because new productions attracted larger audiences than previously displayed

¹⁹ The records of the Biograph company indicate that between 1900 and 1906, 1035 of 1809 films produced were non-narrative—see Spehr (1980, 421). As late as midway through the first decade, documentaries were still a staple—Allen (1985, 75-76) says that documentary films (travelogues and newsreels) made up half of all American films produced between 1904 and 1906.

²⁰ Photographs of early nickelodeons, such as in Merritt (1985, 84 and 90) and Gomery (1992, 121) show either no film titles advertised, or the title listed on small placards, while large letters were used for such general announcements as “High Class Motion Pictures & Illustrated Songs,” and “Motion Picture Subjects, 5 cents.”

²¹ See, e.g., Balio (1985a, 16), and Donahue (1987, 7).

²² The nickelodeons switched films at least weekly, and sometimes several times per week. The typical “show” consisted of a number of short films, lasting altogether for between thirty minutes and one hour. The audiences were also often treated to live entertainment: singing, music, and other performances. See Merritt (1985).

²³ By 1907, between 125 and 150 exchanges operated around the country. See Balio (1985a, 17).

²⁴ The following is from testimony given before the Federal Trade Commission in the 1920s: “The practice of block-booking, in its essential substance, has been rooted in the industry since its inception. The practice is directly evolved from the old service idea, under which entire programs were furnished to exhibitors, and which is frequently referred to as the ‘program system.’” (Lewis 1933, 147).

films, producers began to charge higher prices for prints of new releases, and to sell them on a subscription basis only. Each exchange signed a standing order with one or more movie producers for the weekly delivery of the producer's "program", i.e., for at least one print of every new picture the producer made.²⁵ The system was not controversial; many hours of film were required to meet the need for frequent program changes. Given the relatively undifferentiated nature of the product (several minute views of landscapes, passing trains, public speeches, and prize fights), it was simpler and cheaper for all concerned to commit to buy whatever was produced (indeed, they had to in order to fill screen time) than to choose film prints one-by-one from a catalog.

Between 1905 and 1910, film-makers gradually switched from documentaries to narrative subjects. Narratives were easier to make; the storyline could be geared to the limitations of studio and surrounding locale. However, the quality of individual films remained low. The films often failed to tell clear and comprehensible stories, and instead focused on such things as magic tricks or chases, which could be sold in detachable units.²⁶ The preferred fare was slapstick comedy, usually violent.²⁷ The "star system" had not yet developed; actors were not even credited for their roles, and would not be for several more years.²⁸ Technology, rather than artistic or narrative skill, was considered central to success, and producers sought to differentiate their pictures by emphasizing the technical superiority of the production and exhibition equipment, rather than the narrative superiority of the films.²⁹ As late

²⁵ Section 5 of a typical exchange agreement specified that the exchange would receive "one or more prints of each and every subject regularly produced and offered for release by such manufacturer or importer." See Cassady (1959, 36), quoting from the court record.

²⁶ A 1911 trade paper critic commented of one-reelers that "There is too much evidence of 'cutting up' and 'cutting off' to the detriment of the continuity of the pictures, and this slaughtering of the subject only increases the ambiguity of the whole." Quoted in Staiger (1985, 176).

²⁷ The following plot descriptions pertain to popular one-reelers of 1908: two Irishmen at a lodge initiation fight each other with bricks and dynamite (*Casey Joined the Lodge*); two boys awaken a daydreaming policeman by setting him on fire (*A Policeman's Dream*); a political candidate has dirt and paste thrown at him, then his wife beats him (*The Candidate*); partygoers fall into a young gentleman's room when the floor caves in, and are beaten (*Noisy Neighbors*). See Merritt (1985, 88).

²⁸ In fact, cameras were typically fixed in a static medium-long shot that left the faces of the actors difficult to distinguish—See Kerr (1990, 388).

²⁹ For example, in 1909 the *New York Dramatic Mirror* sang the praises of the Selig Film Company as follows:

as 1911, writes Ralph Cassady (1959, 371), “there was relatively little preselection of subjects by exhibitors.” The General Film Company, which dominated film distribution between 1910 and 1912, described its leasing practice as follows:

no account was taken of individual pictures or of individual actors or directors, and the flat rate per foot applied without regard to the number of separate pictures, the quality or character of the pictures, the size of the theater, or the town or city.³⁰

In sum, when the first block selling arrangements emerged, the movies they contained were highly homogeneous. While audiences may have responded more favorably to some than to others, films were short and quality was uniformly low.³¹ As a result, all films were sold at the same price, by the foot, just like a grade of lumber or bushels of wheat. Furthermore, no new information was revealed between the signing of the contract and the receipt of (and payment for) the films. In short, there was no potential oversearching problem of the kind Kenney and Klein suggest motivated block booking.

As time passed, films changed. The biggest innovation was the appearance of the “feature film,” a multiple reel effort that lasted one hour or more and was first seen among movies imported from Europe around 1911.³² Between 1912 and 1914, nearly three hundred feature films were distributed in the United States,³³ and by 1915, the feature film was the norm.³⁴ Feature films were rented, rather than sold outright, and required a concomitant change in distribution and exhibition practices. The nickelodeons, where single reel films were shown, were generally too small to generate revenue sufficient to support the more expensive and much longer feature films, and were

There are several big dynamos to supply electric light and power, and in the far corner of the plant is a machine shop where inventors are constantly at work making improvements in projection and other details. . . . There is a most efficient staff and work proceeds in a most systematic manner. There is . . . nothing wanted to make the best moving picture shows made anywhere on earth.

Quoted in Kerr (1990, 392).

³⁰ Lewis (1933, 7)

³¹ In fact, the films were sometimes so bad that vaudeville theaters used them as “chasers;” they were played when the operators wanted to clear the house for a new group of patrons—see Allen (1985, 71).

³² See Staiger (1985)

³³ Balio (1985b, 111).

³⁴ D.W. Griffith’s classic, *The Birth of a Nation*, opened on March 3, 1915 in New York and ran there for 802 performances; it broke box office records wherever it was shown (see Balio 1985b, 112-113).

gradually supplanted by larger theaters. However, the exchange system of distribution was based on selling to nickelodeons. To serve these new, larger cinemas, the first national film distributor, Paramount Pictures, was formed in 1914 by the merging of eleven territorial exchanges.³⁵ It began by formally grading theaters from first to fifth-run, based on size, location, and condition.³⁶ First-run theaters exhibited films first; they were located in prime downtown areas, were large and elaborate, and showed new releases for a week or more. Fourth and fifth-run theaters were located in residential neighborhoods, showed films that had already been on the market for several months, and changed their films several times per week. The second and third-run theaters fell between, being located in busier areas and exhibiting films for 1-4 days. Theaters within each run designation enjoyed a contractually-set period of time that had to pass before a film could be sent to a lower run theater (the “clearance”). For example, second-run theaters usually had to wait for three weeks beyond the end of the first-run showing to exhibit a film, and so on down the line. Finally, runs and clearances operated within a specified geographic “zone,” over which the exhibitor was given exclusive privilege.³⁷ This categorization of cinemas into runs and stipulation of clearance periods and zones quickly became the industry standard.³⁸

The avowed goal of Paramount’s first president, William W. Hodkinson, was to establish a system that would guarantee exhibitors a steady flow of product.³⁹ Paramount distributed 104 films per year in its first few years, enough to fill the playing time of houses that changed programs twice per

³⁵ Two alternatives preceded Paramount: selling film rights territory by territory to buyers who rented them out for a flat fee (the “state rights” method), and film exhibitions arranged by the producers themselves, who booked theaters on a one-off basis for a percentage of the gross revenues (“road shows”). Often, the film would be road shown in big cities, and then the rights would be sold territory by territory for the rest of the country. While these approaches worked fine for individual pictures, they were too cumbersome and costly for the distribution of film in quantity. See Balio (1985b) for a discussion.

³⁶ Why Paramount first did this is open to question; it may have been a variation on the old vaudeville booking process—a new act would open at a flagship theater and then move to other houses in order of prominence. See Allen (1985)

³⁷ Zoning eventually became quite complex, and even gave theaters in certain cities prior rights over those in other cities. See Huettig (1944, 125-7).

³⁸ It was this system that created the oversearching problem: first-run results were available before subsequent-run cinemas received and paid for films.

³⁹ See Berg (1989, 49)

week. Its variation on the old program system became known as “block booking.”⁴⁰ Block booking and program selling differed in that the former involved a contract for a precisely-defined “season” (initially three months; eventually, a full year), while the latter was a weekly arrangement of indefinite duration; however, in each case, the exhibitor contracted for a producer’s entire output, or some part thereof. The evolution from service system to block booking occurred in several steps. Paramount initially provided exhibitors with a simple list from which they could choose as many films as they wanted, with all films rented at the same price (although that price varied with the size of the exhibitor’s town).⁴¹ Paramount (and its rivals) then began to set up film blocks around movie stars, and to charge higher prices for the blocks of the more popular stars.⁴² Finally, star blocks were abandoned in the early 1920s in favor of the more flexible general blocks that would characterize block booking thereafter—an exhibitor could book as many films as it desired from the producer’s entire offering, at prices that varied with the expected popularity of the film.⁴³ Although producers preferred to sell as large a block as possible (i.e., to include as many of its films as possible) to any given exhibitor, the size was negotiable.⁴⁴ However, the greater the number of films an exhibitor contracted for, the better the terms it received.⁴⁵

⁴⁰ See Balio (1985b, 117)

⁴¹ For example, in 1917, an exhibitor in a town of 10,000 could book as a pictures for \$37.50 for one day, \$45 for two days, and so forth, while an exhibitor in a town of 5000 could book the same picture for \$25 for one day, \$30 for two, and so forth. See “Federal Trade Commission” (231)

⁴² The following description of “star blocks” was given during testimony before the Federal Trade Commission: “The names of the particular pictures were still of no importance and the pictures were sold merely by the series or blocks in which the same star appeared. . . . [T]he exhibitor bought, for example, 6 Pickfords, 6 Harts, or 6 Clarks.” See “Federal Trade Commission”, 232

⁴³ The 1939 MGM product offering, for example, consisted of four “super-specials” on which the rental rate was forty percent of revenue; ten “lesser bombshells” with a thirty-five percent rental rate; another ten films at a thirty percent rate, and twenty B-pictures, mostly at flat rentals (these were used primarily as second features). See *Fortune*, vol. 20, pp 25-30, August 1939. Ricketson (1938, 32-33) lists the following hypothetical package of 52 pictures as typical: 4 pictures at 35 percent of gross receipts (which would revert to 30 percent if the theater did not earn one-third of film rental paid on each individual picture as profit), 6 pictures at 30 percent (falling to 25 percent under the same conditions), 12 pictures at 25 percent, and 30 pictures at flat rentals. He notes that the charges might fluctuate by plus-or-minus 5 percent, depending upon the size and bargaining power of the exhibitor.

⁴⁴ Some have described block booking as an “all or none” agreement (see, e.g., Cassady 1933, 120), but this was clearly untrue. For example, only half of all contracting exhibitors took the entire 1939 MGM line mentioned in the *Fortune* article (see the previous footnote), while fewer than 20 percent of 20th Century-Fox’s 1938-39 exhibitors accepted its full block of fifty-two films (1940

Blocked films were sold “blind”; i.e., exhibitors were not provided with the opportunity to view the films before signing the contract (this was of course the practice with the program system as well). “Blind selling” is actually somewhat of a misnomer; exhibitors usually knew the titles, casts, and directors of the films they booked.⁴⁶ The rationale for selling blind was straightforward—it saved on inventory costs.⁴⁷ However, although the films were *contracted for* blind at the start of the season, they were not *paid for* until actually exhibited, usually some months later.⁴⁸ By this time, first-run receipts (at least) were observable, which created the problem described by Kenney and Klein.

The first block booking contracts (in contrast to later practice) specified *exactly* which films were being leased, and an exhibitor was not required to show any film based on a different script or featuring a different star or director than specified at the time of the agreement (this would change). Furthermore, any film that was believed offensive to local audiences could be removed from the block at no penalty, given approval by an arbitration board.⁴⁹ Finally, these early contracts included the right to cancel up to fifty percent of the package at no penalty once the first-run results were available.⁵⁰

The introduction of sound in the late 1920s led to the a switch from flat rentals to revenue-sharing as the predominant form of exhibition payment,⁵¹ but film prices continued to vary with the

Congressional hearings, cited in Kenney and Klein, 518). And of 322 separate Paramount contracts signed with plaintiff exhibitors for the 1920-21, 1921-22, and 1922-23 seasons, only 31 were for the entire block of Paramount films offered, while 98 were for a single picture each (see Lewis 1933, 157, citing testimony before the Federal Trade Commission).

⁴⁵ See, e.g., “Federal Trade Commission” (1930, 228). This also suggests a selling cost-based explanation for block sales.

⁴⁶ In fact, even had it been possible to preview the films, exhibitor choice would have been “blind” in the sense that audience response would have remained unknown.

⁴⁷ See Kenney and Klein (1983, 521).

⁴⁸ For films rented on a percent-of-gross revenue basis, payment was due upon the last day of showing, or at the end of each day, if the producer so desired. For films rented out for a flat fee, payment was officially due three days before receipt of the print, but in fact was also often paid after the showing. This information is taken from contracts between the Warner Brothers Company and various independent theaters (see section IV), as well as from descriptions in Ricketson (1938, 30-31) and Lewis (1933, 181-200).

⁴⁹ See Donahue (1987, 22). Of course, the arbitration process may have been costly.

⁵⁰ See Huettig (1944, 120).

⁵¹ See Hanssen (1999) for an investigation of that change.

expected performance of the film.⁵² Revenue-sharing was used only for “A” (major) films; low budget “B” films continued to be leased for flat fees. It was also applied only to first-run through third- or fourth-run theaters no matter what the film.⁵³

Thus, by the time of the *Paramount* decision in 1948, the conditions outlined by Kenney and Klein were in place. Did block booking prevent oversearching, by forcing exhibitors to accept ex post all (or substantially all) films booked ex ante? To say more, I will turn to the nature of the optimization problem between producers and exhibitors, and the details of block booking contracts.

IV. THE OPTIMIZATION PROBLEM AND BLOCK BOOKING

The challenge facing film producers can be portrayed most straightforwardly by imagining that they are fully integrated into exhibition; many of them did indeed own theaters.⁵⁴ Imagine as well that there is only one producer/exhibitor, and it has only one film. It does not know how good or bad that film is—i.e., how much revenue it will generate—until the film is actually shown to the general public. By that time, most of the costs associated with the film are sunk; advertising and exhibition costs being the exception. Therefore, the producer/exhibitor shows the film for as long as it can cover its direct exhibition costs.

If the producer/exhibitor has another film in its warehouse, the cost of showing film 1 is not simply the monetary expenses associated with exhibition, but the lost opportunity to show film 2 instead. Assume for simplicity that films are of two quality types: “low,” which generates \$1 per day, and “high,” which generates \$2 per day. All marginal costs associated with exhibition are 0. The

⁵² For example, the 1937 MGM film *Test Pilot* with Clark Gable, Myrna Loy, and Spencer Tracy rented out at 40 percent (to the producer), while the same company’s 1937 film *Man Proof*, also with Myrna Loy but co-starring lesser lights Franchot Tone and Walter Pidgeon instead went for only 30 percent (information taken from Warner Brothers booking schedules—see section IV). “Sliding percentages,” whereby the rental rate increased as revenue increased, were also occasionally used.

⁵³ The reason for the first exception was that B films were primarily second features—double features were standard in the 1930s and 1940s—and showing two films on a revenue-sharing basis would have made it costly to determine the individual contributions of each. Small theaters did not lease on a revenue-sharing basis because the cost of monitoring to ensure honest reporting of attendance was too high relative to the revenue produced. For more detail, see Hanssen (1999).

producer/exhibitor then shows one film for a day, and if it generates \$1, knows it is of low quality and immediately replaces it. If it generates \$2, the exhibitor knows it is of high quality and lets it play.

Of course, a film does not generate a fixed level of revenue indefinitely—the audience for any single film declines over time, as more and more of those who want to see it actually have.⁵⁵ For that reason, a large numbers of films are produced annually, and we see a regular turnover of features as time passes. Producer/exhibitors have cutoff points at which an old movie will be replaced by a new one. How quickly that cutoff point is reached depends on the film; today, highly popular films play for months, while unpopular ones may disappear in a week. With this additional twist, the optimization problem is the same as in the previous scenario, and the producer/exhibitor will adjust film playing time in line with demand.

If we drop the assumption that producers and exhibitors are one in the same, does the conclusion change? No. Given that films are priced on a revenue-sharing basis, producer and exhibitor still both desire to see popular films play for longer than unpopular ones.⁵⁶ They both therefore have the incentive to devise the most efficient (in terms of maximizing the joint profits, or revenues, given the mostly fixed-cost nature of the business) contract possible; they then can divide the rents that accrue.

The story changes somewhat when the possibility that there are several competing film producers is considered. As the audience for a particular film dwindles, the exhibitor still wishes to change it for another film. If that other film is the product of the same company as the original film, then the producer will share the desire; however, if the replacement instead comes from another studio, the producer prefers to see its original film keep playing instead, at least for the duration of the contracted period.

⁵⁴ See De Vany and Eckert (1991) and De Vany and Walls (1996, 1997) for a more detailed discussion of the optimization problem. See Huettig (1944, 31-38) for a brief history of the integration of production and exhibition.

⁵⁵ See De Vany and Eckert (1991)

The movie distribution contract thus had to balance the need for flexibility with the risk that the exhibitor would use that flexibility to opportunistically replace the films of one producer with those of another producer, in the manner that Kenney and Klein suggest. How did the contracts do this? To answer that question, I investigate contracts of the time. The University of Southern California Film School maintains an archive of material from the Warner Brothers Company. Recently, several hundred boxes of exhibition contracts and various other bits of information relating to film exhibition were discovered in a New York building that was being demolished. Archivists are still cataloging much of what was found, but they allowed me access. From that material, I obtained complete 1937-38 schedules and box office receipts for all first, second, and third-run theaters owned by the Warner Brothers Company in the state of Wisconsin—twenty-eight theaters that played collectively more than 5000 films in that period.⁵⁷ Those schedules provide information on the number of days each film was booked, the number of days each was actually shown, the revenue earned, and the applicable pricing arrangements.

Tables 1 through 3 summarize some of this information. Table 1 divides the films into two categories: those booked for a fixed number of days (1,2, etc.) and those booked instead for a range of days (1-2, 2-3, etc.). The vast majority of films fall into the latter category. This makes sense: *ex ante*, one can predict only very imprecisely how a film will be perceived, but once the showing has begun, new information is learned that may make either extending or abbreviating the performance desirable. The most frequent contract in the sample was a two-to-three day booking (typical for a second or third-run theater), although two-to-four and three-to-four were also common. However, the flexibility did not end there: abbreviations and extensions *outside* the contracted range were also allowed. Table 2 relates the number of days a film was booked to the number of days it actually played. Only a bit

⁵⁶ In fact, the long term incentives should be the same even with flat rental fees, because the amount an exhibitor will pay depends upon the amount of revenue that will be generated. However, in the short-run, a producer has a stronger incentive to extend a poor film's run if it is receiving a flat payment than if it receives a share of the revenue.

⁵⁷ Like most producers, the majority of Warner Brothers cinemas were first-run. However, by historical accident (they purchased several producer/distributors) they retained holdings of second and third-run theaters in Wisconsin. See Beaver (1983, 146-151) for a short history of Warner Brothers. The booking practices for these producer-owned chains do not appear to have differed in important

more than seventy percent of films played for their contracted period. Eighteen percent were taken off the screen more quickly than the contract called for, while nine percent played for longer.⁵⁸

In short, films were booked for a range of days rather than a fixed period, and adjustments of that range were frequent. As a result, the runs of popular films could be extended and unpopular ones abbreviated, to the benefit of exhibitor and producer alike.⁵⁹ Of course, this meant that neither the exhibitor nor the producer knew *exactly* how many films would be required in the course of a year.⁶⁰ Producers therefore had to permit the *ex post* rejection of films from the contracted-for block; otherwise, exhibitors would hesitate to extend popular showings, out of concern that they would run out of time before they ran out of films. And, indeed, *ex post* rejections were allowed. Most prominently, block booking contracts contained a “cancellation clause,” which granted exhibitors the right to refuse a given number of films from the block *after* actual box office receipts were reported.⁶¹ *Variety*, the industry newspaper, even ran weekly reviews of film receipts by city intended to help exhibitors decide which films to accept and which to cancel.⁶² Film exhibitors could use the

ways from those of independent chains—see discussions in Lewis (1933, 71-5). For example, Lewis (110) describes how RKO’s own theater division had the right to refuse to accept any RKO film that it considered “unsuitable” for exhibition.

⁵⁸ There were 575 days of showing in excess of the original contract period, and 1285 days of shortened showings.

⁵⁹ I examined the relationship between days played and revenue earned by estimating a simple Ordinary Least Squares regression, with per day revenue as my dependent variable, the number of days the film played as my variable of interest, and a dummy variable for weekend or holiday, the run designation, and theater dummies for each of the twenty-eight cinemas as control variables. Only “A” films—those booked on a percent-of-gross basis—were included in the sample. I found each extra day of showing to be associated with \$86 of additional per day revenue, nearly one-quarter of that of the average (the average film in this data set grossed \$379 per day). The coefficient had a t-statistic of nearly 17.

⁶⁰ It also meant that contracts had to be quite vague on exactly *when* an exhibitor received a given film, since if earlier-run theaters varied the number of days they kept a film (as they evidently did) no one could know for sure when that film would be ready for subsequent-run use. And so the contracts specified no dates, but instead promised simply to provide the exhibitor with fifteen days notice of available play times and a thirty day window within which it could choose its preferred dates. At regular intervals, the producer’s “booker” sent out notices of availability, which listed the current productions contracted for by each exhibitor and the dates available for showing. See Lewis (1933, 58) for a description.

⁶¹ The cancellation clause is discussed in Donahue (1987, 25), Huettig (1944, 120), and Whitney (1982, 167).

⁶² See Klaprat (1985, 355). Howard Franklin (1927, 27), President of Fox Studio’s West Coast theater holdings, described first runs as “affording independent theater owners an opportunity to gauge the public reaction to pictures presented, and serving as a guide to value.” Perusing old issues of *Variety*, one finds such headlines as “*Narrow Street*, 2nd week, \$13,650; Only Fell Off \$200 at Piccadilly”, “*Women Off Greed*; \$9000 in Washington”, and “*Narrow Street* Liked But Got \$8000—*So Big* at \$12,000”, all from the

cancellation clause to adjust, at the margin, the number of films they actually accepted, and thus vary play dates in line with demand without worrying that they might not be able to show all the films they contracted for. The cancellation clause was a standard feature of block-booked contracts, and ten percent was the standard minimum.⁶³ Paramount's early block booking contracts had included the right to cancel up to *fifty percent* of the package at no penalty once first-run results were available.⁶⁴

The cancellation clause was, in fact, only one of many sources of ex post adjustment of film exhibition obligations. FBO Productions (soon to become part of RKO) conducted a study in which it charted all non-penalized cancellations for two weeks in November 1927, two weeks in February 1928, and one week in March 1928, and categorized them by cause. Table 3 reproduces that information.⁶⁵ The first cause listed in category 1 makes perfect sense: the substitution of one of FBO's productions for another (presumably an unsuccessful picture for a successful one)—this benefitted FBO and exhibitor alike. Cancellations were also permitted where pictures were deemed “unsuitable” to the exhibitor's audience,⁶⁶ where the exhibitor wished to trade old pictures for new (more on this directly below), as well as for more mundane reasons, such as bookkeeping errors, violations of territorial promises, and theaters failing to open. The cancellation clause is listed, too (cause 4 in category 1), but so are shortened runs and lack of open dates, each considered sufficiently frequent occurrences to include them among the causes of cancellations. Interestingly, exhibitors were also permitted to cancel films when the price was simply revealed ex post to be too “high” (cause 10 in category 1). This is not as surprising as it might first appear—FBO dealt with the same exhibitors year

January 21, 1925 issue. In the December 11, 1934 issue, one reads, “*Divorcee* Big in Denver, \$10,000”, “*Monte Cristo* Holds Second Week in Birmingham Despite All”, and “*Veil* \$8000 in Seattle; *Life* \$5400”. The articles list revenue totals for first-run showings in all the major cities around the United States.

⁶³ The following is taken from the Standard Exhibition Contract (see *The 1929 Film Daily Yearbook*, 801-815):

Twentieth: The Exhibitor shall have the right to exclude from the contract up to but not exceeding ten percent of the total number of such photoplays, but only if the Exhibitor shall give the Distributor written notice to such effect at any time not later than fourteen (14) days before the date fixed for the exhibition.

⁶⁴ See Huettig (1944, 120).

⁶⁵ See “FBO Productions” (1930, 399-400), exhibits 3 and 4.

⁶⁶ This was specified in the Standard Exhibition Contract, twenty-first clause (see *The 1929 Film Daily Yearbook*, 801-815).

after year, and repeat dealings provide a substantial incentive to take the interests of the other party to the transaction into account.⁶⁷ However, it does not suggest an overwhelming concern with limiting ex post search.⁶⁸

Contractual flexibility is further demonstrated by the practice of “rolling over” unshown films into the following season, common in the industry at the time. Most of the rolled-over films were never actually shown, but were instead exchanged for agreements to show newer films. Table 4 illustrates, again for FBO.⁶⁹ The top row lists the percent of the 1927-28 exhibitor film obligations by the year in which the film was released. As one would expect, the majority of booked films pertained to that same season; however, 14 percent were from the previous year, and 4 percent were from even earlier. The FBO study (395-6) states that “Sometimes these [rolled over films] were pictures which the exhibitors considered of unsatisfactory quality and, therefore, had neglected to select dates for, hoping that an opportunity to cancel them would present itself. Sometimes the exhibitor had contracted for too many pictures, and had not had time to exhibit all of them.” And as row 2 of table 4 indicates, between July 2nd and December 2nd of 1927, 42 percent of the obligations from the 1926-27 season, 63 percent of the obligations from the 1925-26 season, and 73 percent of the obligations from the 1924-25 season were canceled in return for booking films from the 1927-28 season (two percent of that year’s films were exchanged for other FBO productions, as well). The study notes that, “[E]very member of the sales organization knew that a large proportion of all cancellations consisted of adjustments made to exhibitors to further the sales of the new season’s pictures.” (395) Such cancellations were a loss for accounting purposes only; the study continues, “They [FBO’s management] knew that the exhibitor had

⁶⁷ See, e.g., Klein and Leffler (1981). This was done in other ways as well; for example, De Vany and Eckert (1991) point out that film companies made ex post adjustments to rental terms when a block of films performed particularly badly (see also Cassady 1958, 176-77). Producers continue to do such things today (see section V and Kenney and Klein, 530).

⁶⁸ The categorization is insufficiently fine to determine what percentage of cancellations are explained by each cause individually; however, one can get a sense of the importance of the cancellation clause alone. If I ignore categories 3 through 6 (which involve causes of a different kind), category 1, which includes the cancellation clause, accounts for 69 percent of all cancellations. That means that even if the cancellation clause explains as many as three-quarters of the total in category 1, it still accounts for only half of all the cancellations that occurred during the period. FBO’s sales manager estimated that total cancellations amounted to 17 percent of sales on average—see “FBO Productions” (395).

⁶⁹ See “FBO Productions” exhibit 1, pp 392-3

only so many days in the year to show pictures and that if all the time was taken up, the mere substitution of new pictures for old pictures was not a real loss of business.” (396)

Exhibition contracts were thus extremely flexible, which suggests that block booking was not intended primarily to force exhibitors to respect their *ex ante* exhibition obligations—given the flexibility, it could not have served that purpose. But did exhibitors at least attempt to redistribute income from producers to themselves *ex post* to the extent that contracts allowed? If I find that they did not, it sheds further doubt on the hypothesis that block booking, itself, was necessary to keep oversearching in check.

First, I can conduct a simple test by examining the use of the cancellation clause. If the *ex post* rejection of low quality films was limited only by the terms of the written contract, I should find the cancellation clause consistently evoked up to its maximum (or close thereto). However, if the clause instead existed primarily to allow programs to be adjusted at the margin, it being difficult to predict precisely the number of films needed per year, I should occasionally (at least) find fewer than the allowable number canceled. If I see that exhibitors were persistently failing to take advantage of contractually-permitted opportunities to rid themselves of the worst-performing films, that sheds doubt on the premise that block-booking existed solely to prevent such behavior.

In the Warner Brothers archive, I obtained a number of contracts from the 1930s and 1940s between the Warner Brothers studio and several independent exhibitors in the Long Island area.⁷⁰ These provide information on canceled films, which is summarized in table 5. Eight theaters altogether are represented, for a total of sixteen theater-years. The third column lists the number of films canceled during that year, the fourth the number of cancellations allowed by contract, and the fifth, the difference between the two. The cancellation clause was used to its fullest in only four out of the sixteen possible cases.⁷¹ Of the 98 possible cancellations, only 61 were invoked. Cinemas left 3, 4, 5,

⁷⁰ The boxes also contained contacts from the 1950s, by which time block-booking was no longer used, and contracts from earlier periods that made no mention of the cancellation clause.

⁷¹ The reader will note the absence of negative values; i.e., of instances when more cancellations occurred than was contractually permitted. This is due to the nature of the data. There are seven cinemas not included in the table for which I have information on the

and even 7 cancellations unexercised, a substantial amount of foregone ex post search. Of course, a theater would be unwise to use up its cancellation options prematurely, but the numbers of cancellations left unexercised by the various exhibitors appear to be greater than a simple careful use of cancellation options would suggest.

I will conduct a second test: I will compare the number of days of film initially contracted for to the number of days of playing time actually available. The Kenney and Klein hypothesis suggests that if given the opportunity to reject films from the block ex post, exhibitors will contract ex ante for more films than they can actually use.⁷² At the extreme, one can imagine an exhibitor booking *all* available films, and simply keeping those revealed ex post to be the best. Of course, cancellation privileges were not unlimited; nonetheless, if it is indeed *solely* (or even primarily) the terms of the block contract that prevent this form of oversearching, I should find that theaters engaged in it to the degree that contracts allowed.

I look for evidence among the Warner Brothers theaters whose contracts are summarized in tables 1 through 3. I will compare the number of days of film actually exhibited (which represents the amount of showing time available) to the number of days of film booked at the start of the season. Because most contracts were for a range rather than a fixed number of days (see table 1), I will compare available days to the minimum and maximum days contracted for, as indicated by the low end and the high end of the agreed range. I will conclude that overbuying occurred if the minimum ex ante contractual obligation is greater than the number of available days.

The results are shown in table 6. The sample consists of the twenty of the twenty-eight theaters for whom the entire 1937-38 season's bookings are available.⁷³ As the top row shows, although there

number of films canceled from the original block, but not the number of cancellations allowed by the contract in total. In each case, the number actually canceled was in excess of ten percent of the total number booked. If ten percent was indeed the contractually-specified amount (which, I believe, is a reasonable conjecture) then those cinemas would list negative values. But because I do not have the specific terms of the cancellation clause for these cinemas, I have left them out of the sample.

⁷² This is simply "overpricing" in a revenue sharing context (see footnote 10 above).

⁷³ "Entire" in the sense that bookings from each of the eight major film companies (Columbia, MGM, Paramount, RKO, 20th Century Fox, United Artists, Universal, and Warner Brothers) are available. The other eight theaters are missing information pertaining to

were 12,299 available days among all these theaters during 1937-38, only 10,812 days of films (minimum) were booked—certainly not evidence of overbuying. The totals for the individual theaters are listed on the following rows.⁷⁴ For only four of the twenty cinemas was there overbuying (in the sense of booking a minimum greater than the available number of days), and in two of those cases, the overbuying was by less than three percent. In three of the twenty cases there was actually “underbuying.” It appears that cinemas were passing up contractually-permitted opportunities to behave in the way that Kenney and Klein posit block booking was necessary to deter.

Finally, as noted above, it is clear (given revenue sharing) that a producer benefits when showings of its films can be adjusted in line with demand, *except* if exhibitors use that contractual flexibility to replace the producer’s own films with those of its rivals. In other words, *intra*-producer flexibility was desirable as far as producers were concerned, while *inter*-producer flexibility was not. The contracts did not specify between them. Which was occurring?

Table 7 compares days booked to days actually played by film studio for all twenty-eight Warner Brothers cinemas. For each of the eight producers, actual days played were in excess of the minimum number booked. For five of the eight, days played were between 15 and 20 percent above the minimum booked, while United Artists and Universal were between 24 and 28 percent above (each sold substantially fewer days of film).⁷⁵ The smallest gap between minimum days booked and days played is for Warner Brothers, but since Warner Brothers owned the cinemas, *ex post* opportunism does not appear a likely explanation.

In short, there is little in the way that contracts were applied to support the Kenney and Klein hypothesis. First, substantial *ex post* substitution away from poorly performing films was allowed (as

particular companies—there would be complete data on all MGM and Paramount bookings, for example, but nothing on RKO bookings.

⁷⁴ The number of available days varies by theater in part because some cinemas tended to close for several weeks in the summer, in part because not all showings were double features, and in part because cinemas varied in the number of B-films they bought from minor producers to show as second features.

⁷⁵ United Artists only distributed the films of affiliated producers, while Universal was, along with Columbia, much smaller than the “big five” producers.

revenue sharing would lead one to expect), while Kenney and Klein suggest that block booking existed to *prevent* exhibitors from doing this. Second, exhibitors evidently failed to take advantage of contractually-permitted opportunities to oversearch, suggesting that the contractual terms (i.e., the block contracts) were not a binding constraint on such behavior.

V. THE AFTERMATH OF THE *PARAMOUNT* DECISION

What happened once block-booking was banned—what took its place?⁷⁶ The question is not as straightforward as it sounds, because block-booking was only one of several practices outlawed by the *Paramount* decision. Movie producers were also required to sell off affiliated theaters, forbidden from entering into franchise arrangements with other theaters, and prohibited from maintaining any fixed system of runs, clearances, and zoning. And there were changes in other things, as well, the most significant being the rise of television. What can be observed in the aftermath of the *Paramount* decision is that the number of films produced fell—in particular, studios stopped making the “B” movies that had supported double features. Movie attendance fell as well.

Despite these changes, producers and exhibitors faced the same challenge as before: getting films to theaters in the right quantities. In the immediate aftermath of the *Paramount* decision, producers experimented with leasing films through competitive bids.⁷⁷ The attempts met with many complaints. One exhibitor commented, “[B]uying one picture at a time is a killer. If you are an individual operator, you have to be on the roam maybe five days a week and then try to run the theater at night.” Another exhibitor said, “What is the difference if we buy them one at a time or buy them

⁷⁶ For reviews of the *Paramount* case and decision, see De Vany and Eckert (1991), Conant (1960) and Cassady (1958). Interestingly, although most exhibitors were apparently happy with the system of block booking (see what follows), the unhappy ones had complained to the court that the fewer the number of films they bought, the higher the per film price they were charged. Producers acknowledged that this was so, but defended themselves on the grounds that the fewer the pictures taken, the higher the selling cost per picture (as the argument that block booking was intended to reduce direct selling costs would suggest). See “Federal Trade Commission” (1930) for more detail.

⁷⁷ Any theater interested in showing a particular film at a particular time in a particular area would submit a sealed bid, and the highest bidder would receive the film. The Court did not actually require a system of competitive bidding, but rather prohibited discrimination against small independent exhibitors. However, the only way to be *completely* sure of avoiding the accusation of discrimination was to hold a competitive bid.

together; we still have to play them all.”⁷⁸ Conant (1960, 145) writes that after block booking was banned “[m]any exhibitors . . . found negotiating for each picture individually too time consuming and preferred to buy films in groups.”

Competitive bidding was used primarily in competitive areas; in “noncompetitive” areas (i.e., where a single theater served a well-defined audience) producers could still lease in blocks if the theater so requested, and it usually did. In fact, even in competitive areas, block booking was permissible if all theaters agreed.⁷⁹ As Simon Whitney (1982, 184) notes, “As late as 1958 about half the theaters [in competitive areas] leased some of their films in groups—for the labor of buying would otherwise have been impossibly heavy—although they signed an individual contract for each.” Interestingly, the Allied Association of Motion Picture Exhibitors, a trade association that supported the Department of Justice’s crusade to force the divorcement of production and exhibition, was so unhappy with the disappearance of package selling that it sponsored its own plan. Under that plan, 2400 theaters would have contracted with an independent producer to make a feature film for them each month—a revival of block booking, for which the Justice Department granted an exemption.⁸⁰

The movie distribution business is somewhat different today, in large part because of the rise of the multiplex (the many-screened cinema).⁸¹ Rather than a detailed system of runs, movie studios now release their films widely all at once, on what is called the “national break.”⁸² A “general” (or broad) release entails opening a film on 2000 or more screens at once, while a “limited release”

⁷⁸ Both quotes from Whitney (1982, 184).

⁷⁹ For example, in 1950, 3700 theaters chose to book Paramount pictures in blocks with a right to cancel 20 percent—see *Variety*, September 20, 1950, page 5.

⁸⁰ The plan never came to fruition—see Whitney (1982, 179).

⁸¹ The following draws on conversations with Drew Devlin, President of Clark Film Buying, and on essays by Murphy (1992), Reardon (1992), and De Vany and Walls (1996).

⁸² Some cinemas in smaller towns receive films several weeks after the national release, usually for discounted rental terms. The smallest theaters in the smallest towns still receive films months after the initial opening, and still pay a flat rental fee.

involves 500-1000 screens, with plans to open more later if popular response warrants.⁸³ Films continue to be leased on a percent-of-gross revenue basis.⁸⁴ As before, revenue-sharing means that both producer and exhibitor benefit when the most popular films get the most screen time.⁸⁵ The multiplex now allows cinemas to juggle films, so that seats and screen time more closely conform to demand. A particularly popular picture may open on two or more screens at once, and then be shifted to smaller screening rooms as the audience dwindles over time.

What is the contracting process? Producers provide exhibitors with annual release sheets, which list movie titles, plot descriptions, casts, and projected release dates for the coming year.⁸⁶ Delays occasionally occur, but a film is typically locked into a particular release period (i.e., summer, Thanksgiving/Christmas, etc.) about four months in advance. Exhibitors then rough out a tentative schedule. Because how long a picture shows depends, as always, on how well it is received, the schedule remains very imprecise until quite close to the opening date. Many states require producers to screen their films before offering them for contract; this is typically done 2-4 weeks before the anticipated release. Once the film has been screened, the exhibitor receives a call from the producer's salespeople naming that date and specifying the relevant terms: the percent-of-gross to be charged and

⁸³ See Reardon (1992, 312). *Armageddon*, for example, a high budget, much-hyped film, was released on 3000 screens at once. By contrast, *The Full Monty*, a relatively low budget British film, was originally released on only 500 screens, and those mostly in larger towns. However, as its popularity grew, additional prints were made, and at its peak, it was showing on close to 1000 screens. On rare occasions, an "arty" film may have a single exclusive opening in New York or Los Angeles, and only open nationally once it has garnered sufficient publicity (*Hamlet*, with Mel Gibson, is an example).

⁸⁴ Rates varying according to (1) the perceived importance of the film (big budget films may charge 70 percent, versus 50 or 60 percent for an average film), and (2) how long the theater plays it (rates typically fall by ten percentage point per week for at least the first three weeks). The percent-of-gross is adjusted upwards for very popular films through the use of an allowance for house expenses known as the "house nut." Most films do not garner revenue sufficient to render that allowance meaningful, but big hits like *Titanic* do.

⁸⁵ Film contracts even contain "holdover clauses," which require a showing to continue as long as revenue is in excess of a specified amount. Furthermore, as an anonymous referee points out, distributors may permit a run to be abbreviated, or a film to be double billed, if the film is performing more poorly than anticipated (this also happened in the days of block booking—see table 3).

⁸⁶ Production schedules are tracked by industry newspapers, such as *Variety*, and by the National Association of Theater Owners (NATO), the industry's trade organization.

the number of weeks to be committed to.⁸⁷ Each week, exhibitors examine the previous week's gross and decide which films to keep and which to replace with the newly available films. They then inform the studios' salespeople. The films are ordered on Monday or Tuesday, and the print arrives the following Thursday, in time for Friday's opening (most films open on Friday). No written agreement accompanies the print;⁸⁸ the long-term nature of the relationship again means that each understands its obligations and has little incentive to breach them.⁸⁹

Thus, although the oversearching problem has largely disappeared (because films are released everywhere at once), the prevailing practice bears a remarkable resemblance to the old block booking system. Just as in the days of block-booking, theaters work with the same producers year after year, contracting for roughly the same number of films. Serious contract negotiations occur once per year at most. Films are accepted as they are released, and play a variable amount of time, depending on demand. A film may occasionally be refused altogether if its anticipated performance is sufficiently poor—parallel to block booking's cancellations. But by and large, most of what is produced gets played without movie-by-movie haggling. The major challenge remains getting films to exhibitors in large and regularly changing numbers at low cost.

⁸⁷ These terms are rarely a surprise—big budget films likely to be highly successful demand the top terms, lesser films lower terms, and so forth.

⁸⁸ Some studios require exhibitors to sign a master agreement at the start of the year, which specifies standard obligations, while others list those obligations in contracts provided on a film-by-film basis. However, the difference is more apparent than real. Under the master agreement system, an order is followed by a confirmation note specifying the terms agreed to. That note generally arrives well after the film has begun to play, and often after the showing has been completed. The contract system instead follows the order with a contract, but that contract is short and of standard form, and specifies no more new information than the confirmation note (the contracts also arrive well after the film has begun to play). In addition, to protect themselves against law suits, most distributors continue to send out bid letters, and negotiations are carried out in the context of a bidding system even when individual dealings would be preferred by the affected exhibitors (or the theater is the only one in the town). I thank an anonymous referee for pointing this out.

⁸⁹ Haggling is rare; similar movies entail similar terms, and producers and exhibitors have a long history of collaboration. As A. Alan Friedberg (1992, 344), Chairman of Loew's Theaters, writes, "Ours is an industry built on relationships evolving from trust, integrity, and loyalty," and then goes on to describe a series of "quid pro quos" between exhibitor and producer.

VI. CONCLUSION

Most analyses of contractual practice focus on a single dimension of a contracting problem. It might be more reasonable to suppose that contractual clauses serve multiple purposes. The question would then be not what single contracting problem explains a particular practice, but rather which of many problems was the practice's primary concern.

This paper has investigated the block booking of films. Several explanations for block booking have been put forward, ranging from the Supreme Court's determination that it allowed movie companies to force exhibitors to buy films they didn't want, to Kenney and Klein's contention that it resolved a measurement problem that would have led exhibitors to opportunistically reject films ex post from a package priced at ex ante average value. The Kenney and Klein explanation is the one most accepted among economists today. However, the problem that Kenney and Klein describe did not exist when block booking first developed, the block booking contract as applied was much more flexible than a primary concern with that problem would suggest, and exhibitors did not appear to take advantage of contractually-permitted opportunities to act in ways that block booking was posited necessary to deter. Instead, the way the practice emerged and the manner in which it was used support the hypothesis that block booking was simply an efficient quantity selling arrangement, as movie producers maintained in their defense.

What did combat the oversearching problem that Kenney and Klein describe? In the first place, there *was* substantial ex post substitution of poorly performing films for better performing films, but with the blessing of producers—because of revenue sharing, producer and exhibitor both gained when film runs could be adjusted in line with demand. However, the flexibility in exhibition contracts went further than that; for example, producers released exhibitors from obligations to show pictures when the price was proved ex post to be “unreasonably high,” or if exhibitors simply had “no open dates.” Such things are exactly what Kenney and Klein hypothesize that block booking was intended to prevent, but, in fact, producers had little to gain by taking advantage of exhibitors. And the reverse was true as well—there were a small enough number of producers given the number of films required that few exhibitors could face the loss of a studio's entire output with equanimity, and things such as run

designation were central to a theater's profitability, and fully under producer control.⁹⁰ In short, there were many potential weapons to be used against exhibitors who abused the flexibility of block booking contracts.

Kenney and Klein recognize that repeat dealings are important, although they do not apply that observation to the oversearching problem.⁹¹ It is clear that whatever the mechanism used to deter ex post opportunism—building reputations for honesty, penalizing errant exhibitors, applying blocks rigidly—there is a cost involved. The cost of rigidly applying block booking would have been a significant decline in the ability of producers and exhibitors to adjust run lengths ex post in line with demand. The fact that such adjustments were common and blocks, as a result, very flexibly applied indicates that other mechanisms were used instead. This is not to say that block booking played no role at all in the process: ex post cancellation rights were not unlimited. However, the analysis conducted here suggests that the problem of oversearching is unlikely to have been the primary concern in the block booking of films.

⁹⁰ Producers and exhibitors dealt with each other year after year, with exhibitors buying roughly the same number of films on an annual basis—Kenney and Klein compare it to a franchise relationship (521). The lawyer for an exhibitor trade association testified in the *Paramount* hearings, “[T]he relationship rests on a long-time course of business between the two parties [producer and exhibitor]. . . and so the two by a course of dealing along those lines built up what somebody has called in his brief a circuitry of friendship. They rely on each other and trust each other in accounting matters as well as in the continued supply of film.” (52-54). Achieving higher run designation's (first, second, and third in particular) usually required substantial investment. Higher-run theater owners were willing to make these investments because the increase in revenue was higher still (see Sharp 1969).

⁹¹ They suggest that rigid block booking reduced the amount of brand name capital producers required, rather than, as here, that the prospect of repeat business influenced *exhibitor* incentives, and thus allowed a *flexible* application of block booking.

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Table 1: Contracting—Fixed versus Variable Number of Days

Fixed Number of Days		Range of Days	
Contract (# Days)	# Films	Contract (# Days)	# Films
<i>1</i>	18	<i>1-2</i>	71
<i>2</i>	111	<i>1-3</i>	4
<i>3</i>	122	<i>2-3</i>	2313
<i>4</i>	234	<i>2-4</i>	880
<i>5</i>	23	<i>3-4</i>	1337
<i>6</i>	3	<i>3-5</i>	98
<i>7</i>	96	<i>4-5</i>	1
<i>total fixed</i>	607	<i>total range</i>	4703

Table 2: Number of Days Played versus Contracted Time

Contracted Days	Actual Days Played			
	<i>< Contract</i>	<i>Contract</i>	<i>> Contract</i>	<i>% Within Contract</i>
<i>1</i>	NA	17	1	94.4%
<i>1-2</i>	NA	59	12	83.1%
<i>1-3</i>	NA	1	3	25.0%
<i>2</i>	30	79	2	71.2%
<i>2-3</i>	380	1823	110	78.8%
<i>2-4</i>	74	711	95	80.8%
<i>3</i>	25	88	9	72.1%
<i>3-4</i>	403	810	124	60.6%
<i>4</i>	19	100	115	42.7%
<i>3-5</i>	17	79	2	80.6%
<i>5</i>	7	15	1	65.2%
<i>6</i>	1	2	0	66.7%
<i>7</i>	10	83	3	86.5%
<i>total</i>	966	3869	477	72.8%

**Table 3: Causes of Cancellation
(FBO)**

Category	Cause of cancellation	Percent
1	<ul style="list-style-type: none"> -Picture of same or previous year substituted for contract picture -Theater did not open -Percentage return overestimated -Exhibitor availed himself of cancellation privilege in contract -Duplication in contracts corrected -Error in contract corrected -Exhibitor revoked contract before receiving approved copy -Same picture previously sold, or now sold, to theater's opposition. -Picture resold to same exhibitor on new contract -Original pricing unreasonably high -Pictures sold for un contemplated run in exhibitor's area 	33%
2	<ul style="list-style-type: none"> -Exhibitor has lowered price scale of theater -Exhibitor claims picture not of suitable type. -Exhibitor used picture for shorter run than contracted for -Exhibitor was ordered by Film Board to assume contracts left by predecessor -Exhibitor demands cancellation of older product in return for buying new -Exhibitor has no open dates -Exhibitor is losing money at his theater -Picture in question was flop at exhibitor's theater -Exhibitor says he has changed type of picture presented by him 	15%
3	Cancellations arising from acts of FBO (no print available, etc.)	2%
4	Theater closed	28%
5	New owner refuses to accept responsibility for contracts of predecessor	17%
6	Accounting adjustments / miscellaneous	5%

Table 4: Cancellation by Year of Release

(FBO)

	Pictures released 1927-28	Pictures released 1926-27	Pictures released 1925-26	Pictures released 1924-25
Percent of outstanding obligations in 1927-28	82%	14%	3%	1%
Percent canceled during 1927-28 in return for new bookings	2%	42%	63%	73%

Table 5: The Cancellation Clause

Name	Year	# canceled	#allowed canceled	difference
Edwards Theater	1933	8	10	2
Hampton Star	1933	3	10	7
Bellaire Theater	1935	6	10	4
East Islip Theater	1935	1	3	2
Bellmore Theater	1936	3	6	3
East Islip Theater	1936	3	6	3
Bellmore Theater	1937	2	6	4
West Hampton	1937	5	5	0
East Islip Theater	1938	1	6	5
Strand Theater	1938	4	6	2
Bellmore Theater	1939	3	5	2
Criterion Theater	1939	5	6	1
East Islip Theater	1939	5	5	0
Strand Theater	1939	5	5	0
Bellmore Theater	1940	4	6	2
Criterion Theater	1940	3	3	0

**Table 6: Days Bought versus Days Available
(Warner Brothers theaters)**

Theater	Days Booked (minimum)	Days Booked (maximum)	Days Available
TOTAL	10812	15394	12299
Egyptian	672	988	683
Garfield	616	947	679
Gateway	408	553	570
Kenosha	560	791	683
Lake	602	871	685
Majestic	467	677	551
Milwaukee	736	1038	669
Mirth	559	821	639
National	687	971	633
Oshkosh	458	679	590
Princess	694	1079	679
Rex	442	615	653
Rialto	394	558	613
Sheboygan	546	773	687
Uptown	612	939	680
Venetian	538	756	677
Vogue	526	763	595
Warner 1	659	659	656
Warner 2	636	916	677

**Table 7: Days Bought versus Days Played—By Producer
(Warner Brothers theaters)**

	Days Booked (minimum)	Days Booked (maximum)	Days Played
Columbia	1337	2055	1531
MGM	2293	3214	2659
Paramount	2104	3059	2382
RKO	1635	2280	1872
20 th Century Fox	1980	2856	2367
United Artists	622	834	769
Universal	877	1445	1119
Warner Brothers	2253	3036	2346