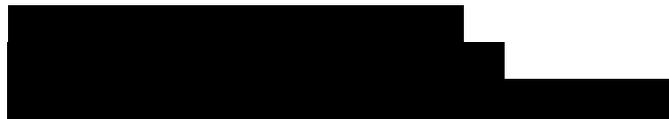




**COMMENTS OF THE NATIONAL ASSOCIATION OF THEATRE OWNERS  
U.S. DEPARTMENT OF JUSTICE, ANTITRUST DIVISION  
REVIEW OF PARAMOUNT CONSENT DECREES**

October 1, 2018



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## I. INTRODUCTION

The National Association of Theatre Owners (“NATO”) respectfully submits the following comments in response to the U.S. Department of Justice Antitrust Division’s (the “Department”) announced intentions to review the Paramount Consent Decrees (the “Decrees”). Individual motion picture theater companies may comment on the five various provisions of the Decrees but NATO’s comment will focus on one seminal provision of the Decrees. Specifically, NATO urges the Department to maintain the prohibition on block booking, as that prohibition undoubtedly continues to support pro-competitive practices.

NATO is the largest motion picture exhibition trade organization in the world, representing more than 33,000 movie screens in all 50 states, and additional cinemas in 96 countries worldwide. Our membership includes the largest cinema chains in the world and hundreds of independent theater owners. NATO and its members have a significant interest in preserving an open marketplace in the North American film industry. North America remains the biggest film-going market in the world: It accounts for roughly 30% of global revenue from only 5% of the global population.

The strength of the American movie industry depends on the availability of a wide assortment of films catering to the varied tastes of moviegoers. Indeed, both global blockbusters and low-budget independent fare are necessary to the financial vitality and reputation of the American film industry. The removal of the prohibition on block booking threatens to undo this system that has enabled our film industry to thrive. If distributors can engage in block booking, exhibitors may be forced to pack their screens with global tentpoles at the expense of targeted programming. Consumers will face increasingly limited choices at the box office, and, without the possibility of a theatrical run, many films will no longer be made, limiting the availability of choices through home entertainment platforms as well.

We wish to use this comment to focus on the importance of the prohibition on block booking as a means of demonstrating how removing this seminal provision of the Decrees could have a profound and negative impact on our nation’s film industry. Not only is block booking illegal,<sup>1</sup> it is bad policy.

Because block booking will be the focus of this comment, we will describe how the Decrees are *more necessary* than ever because of the industry changes described by the Department. We will begin with (I) a discussion on the importance of the Decrees given recent changes to the exhibition and distribution system, then (II) demonstrate that removing the Decrees would

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<sup>1</sup> See Sections II and IV(C) *infra*.

reduce options for content for consumers, then will (III) summarize how removal of the Decrees could reduce competition and incentivize anti-competitive behavior.

## II. CHANGES IN THE INDUSTRY HIGHLIGHT THE ONGOING JUSTIFICATION FOR THE PROHIBITION ON BLOCK BOOKING

In the early days of cinema, film studios began acquiring movie theaters as a means to control the cost and distribution of their films. By 1930, the distribution industry was dominated by five vertically integrated companies that not only produced and distributed motion pictures, but also owned many of the theaters that presented their product to the public.

This control allowed the studios to engage in discriminatory distribution and pricing practices. For example, studios often required independent exhibitors to purchase entire blocks of content, frequently sight unseen, in order to secure a small subset of desirable films with top talent. Small exhibitors who could not afford to book large quantities of film at once, or those who did not wish to pay for films their audiences would not watch, could be forced to opt out entirely.<sup>2</sup>

Theater owners argued that these practices violated antitrust laws, and in *United States v. Paramount Pictures*,<sup>3</sup> the Supreme Court agreed, ending a number of practices and giving rise to the system in place today.

The Decrees specifically prohibited the practice of block booking, which the Court described as “the practice of licensing, or offering for license, one feature or group of features on condition that the exhibitor will also license another feature or group of features released by the distributors during a given period.”<sup>4</sup> The Court agreed with the distributors that intellectual property owners are entitled to a monopoly on an individual copyright, but held that conditioning the licensing of one copyright on the purchase of another—even of equal quality—enlarges the monopoly on each copyright to an anticompetitive degree because the practice “prevents competitors from bidding for single features on their individual merits.”<sup>5</sup> The Court reasoned:

It is said that reward to the author or artist serves to induce release to the public of the products of his creative genius. But the reward does not serve its public purpose if it is not related to the quality of

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<sup>2</sup> Erin Blakemore, *The Hollywood Extortion Racket That Gave Us Today’s Summer Blockbusters*, HISTORY (Aug. 9, 2017), <https://www.history.com/news/the-hollywood-extortion-racket-that-gave-us-todays-summer-blockbusters> (“For other theater owners, it was all or nothing—and those that couldn’t afford 20 or more movies at one time had to opt for nothing. . . . The policy ‘ties the exhibitor hand and foot,’ complained one theater owner in *Outlook* magazine in 1923. ‘He is compelled to show three or four pictures which he cannot truthfully recommend for the sake of one good feature which he will present with no sense of apology.’”)

<sup>3</sup> *United States v. Paramount Pictures*, 334 U.S. 131 (1948)

<sup>4</sup> *Paramount*, 334 U.S. at 156

<sup>5</sup> *Id.* at 156-157

the copyright. **Where a high quality film greatly desired is licensed only if an inferior one is taken, the latter borrows quality from the former and strengthens its monopoly by drawing on the other. The practice tends to equalize, rather than differentiate, the reward for the individual copyrights.** Even where all the films included in the package are of equal quality, the requirements that all be taken if one is desired increases the market for some. Each stands not on its own footing, but in whole or in part on the appeal which another film may have . . . the result is to add to the monopoly of the copyright in violation of the principle of the patent cases involving tying clauses.<sup>6</sup>

The Court held that “a refusal to license one or more copyrights unless another copyright is accepted” was illegal.<sup>7</sup>

The ensuing freedom of exhibitors to book picture by picture formed the backbone of the modern theatrical and exhibition system. Indeed, the success of both the modern multiplex system and the home entertainment market is directly tied to the consumer-targeted programming that has thrived following the prohibition on block booking. That is, *these modern innovations are able to flourish only because of the prohibition on block booking*. To abruptly remove the prohibition on block booking could dismantle the most vital moviegoing culture in the world.

A. Shift to Global Blockbusters Incentivizes Major Studios to Make Fewer Movies While Demanding Longer Runs on More Screens

In the decades following the Decrees, the major studios dramatically decreased the number of movies they produced,<sup>8</sup> making room for smaller studios that were finally able to compete for screen time.<sup>9</sup> In recent years, a focus on globalization has further reduced each studio’s slate as major studios have prioritized global tentpoles: high-budget films meant to ensure high box office profits with mass promotion. In 2002, the six major studios<sup>10</sup> released an average of 23 movies each. In 2017, that number dropped to 14. Indeed, as Disney grew to be the largest studio

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<sup>6</sup> *Id.* at 158

<sup>7</sup> *Id.* at 159

<sup>8</sup> Alexandra Gil, *Breaking the Studios: Antitrust and the Motion Picture Industry*, 3 J.L. & LIBERTY 83–123 (2008) (“Where once each studio was producing upwards of 60 films a year, with Hollywood averaging about 750 films a year in the 1930s, that number was closer to 300 in the 1950s and has continued to decline.”).

<sup>9</sup> Michael Conant, *The Paramount Decrees Reconsidered*, 44 LAW & CONTEMP. PROBS. 79, 92 (1981) (“in a freer market, the minor distributors, who had never been part of the illegal exhibition cartel that dictated first-run theater priorities, became equal competitors with the four surviving majors.”).

<sup>10</sup> Walt Disney Studios, 20th Century Fox, Paramount Pictures, Universal Pictures, Sony Pictures Entertainment, and Warner Bros. Pictures.

in terms of global box office, their slate dropped from 23 films in 2002 to just eight in 2017.<sup>11</sup> It remains to be seen what effect the recently-approved merger of Disney and Fox will have on concentration of power in the market or the number of films released by the major studios. Year to date, Disney has released seven titles and Fox, from all its divisions, nine titles. If the two companies were already combined, their market share of domestic box office as of September 13, 2018 would be 41.7%.<sup>12</sup> Fox has eight more titles to be released in 2018; Disney has three.<sup>13</sup>

There is no doubt that tentpoles bring in large audiences and box office revenues. In 2004, there were 24 films that grossed \$100 million or more, and accounted for \$4.37 billion in revenue and 704 million admissions. By 2014, there were 33 \$100 million plus movies, which brought in \$6.05 billion and 741 million admissions. By 2017, the number of tentpoles held steady at 33, but brought in \$7.25 billion in the domestic box office. Successful franchise films no doubt contributed to 2018's box office surge.<sup>14</sup>

Despite the success of the tentpole model, the shift in focus to the global blockbuster has resulted in a significant reduction in the production and distribution of midrange movies. Filmmakers are similarly increasingly forced to decide between microbudget "passion" projects and big budget blockbuster titles,<sup>15</sup> leaving consumers with fewer options.<sup>16</sup> Between 2004 and 2016, there were fewer titles that grossed between \$50-\$100 million (41 in 2004 versus 34 in 2016), which meant \$436 million less annual revenue and 177 million fewer tickets sold. There were also fewer titles that grossed under \$50 million—81 in 2004 and 76 in 2016—resulting in \$191 million less

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<sup>11</sup> comScore, Inc.

<sup>12</sup> *Id.*

<sup>13</sup> *Id.*; see also Pamela McClintock, *Box Office: Get Ready for Hollywood's Shrinking Studio System*, THE HOLLYWOOD REPORTER (Jan. 4, 2018), <https://www.hollywoodreporter.com/news/box-office-get-ready-hollywoods-shrinking-studio-system-1071457> ("unlikely that Disney would grow its annual theatrical release calendar significantly" after Fox acquisition).

<sup>14</sup> Sean Fennessey, *The Great Moviegoing Fever of 2018*, THE RINGER (July 13, 2018), <https://www.theringer.com/movies/2018/7/13/17567944/moviepass-marvel-star-wars-box-office>

<sup>15</sup> Jason Bailey, *How the Death of Mid-Budget Cinema Left a Generation of Iconic Filmmakers MIA*, FLAVORWIRE (Dec. 9, 2014), <http://flavorwire.com/492985/how-the-death-of-mid-budget-cinema-left-a-generation-of-iconic-filmmakers-mia> ("But slowly, quietly, over roughly the decade and a half since the turn of the century, the paradigm shifted. Studios began to make fewer films, betting big on would-be blockbusters, operating under the assumption that large investments equal large returns. Movies that don't fit into that box . . . were relegated to the indies, where freedom is greater, but resources are far more limited. As *Mad Men*'s Matthew Weiner put it, 'Something happened that nobody can make a movie between \$500,000 and \$80 million. That can't be possible.'").

<sup>16</sup> Pamela McClintock, *Box Office: Revenue Hits Record \$3.3 Billion in Second Quarter, Led by June Bloom*, THE HOLLYWOOD REPORTER (July 1, 2018), <https://www.hollywoodreporter.com/news/box-office-revenue-hits-a-record-33-billion-2q-2018-1124371> ("Disney's dominance underlies what some consider a disturbing trend — it's the big blockbusters holding up the box office, while midrange films suffer."); see also David Robb, *U.S. Film Industry Topped \$43 Billion In Revenue Last Year, Study Finds, But It's Not All Good News*, DEADLINE (July 13, 2018), <https://deadline.com/2018/07/film-industry-revenue-2017-ibisworld-report-gloomy-box-office-1202425692/> ("the majority (54.1%) of all films produced [in 2017] were 'action and adventure' films — tentpole movies designed to attract younger audiences, both domestic and foreign. Only 7.6% were comedies, 15.1% were 'thriller/suspense,' 12% were dramas and 11.2% were 'other' or 'other genres.'").

annual revenue and 104 million fewer tickets sold.<sup>17,18</sup> Studios are having great success with blockbusters, but at the expense of 104 million tickets consumers are no longer buying because the movies they wanted to see are simply not available.

In recent years, new independent and smaller studios have entered the market hoping to bring back the movies—and resulting box office—that the major studios have largely abandoned.<sup>19,20</sup> Exhibitors are eager for these studios and their content to be available on their screens, and therefore screen inventory is essential.

Today, as at the time of the Decrees' execution, the prohibition on block booking is necessary to the effective programming of high-quality and varied programming both in theaters and in ancillary markets. Although studios are making fewer films, these movies still represent the vast majority of the annual domestic box office, granting major studios significant leverage over exhibitors.<sup>21</sup> Absent the prohibition on block booking, studios could require exhibitors to book their entire slate of films in wide release for multiple-week runs. If exhibitors were forced to book out the vast majority of their screens on major studio films for most of the year, this would leave little to no room for important films from smaller studios, or even for breakout hits such as documentaries that achieved mainstream domestic success in Summer 2018 despite competing against big-budget tentpoles. These successes include *Won't You Be My Neighbor?* (\$22.6 million), *RBG* (\$14 million), and *Three Identical Strangers* (\$12 million).<sup>22</sup> This problem would be exacerbated in those markets that have fewer screens per complex. Preserving the prohibition on block booking is vital to the ability of all distributors, both large and small, to bring their movies to the big screen and reap the benefits of a theatrical run.

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<sup>17</sup> *Id.*

<sup>18</sup> Pamela McClintock, *Box Office: Get Ready for Hollywood's Shrinking Studio System*, THE HOLLYWOOD REPORTER (Jan. 4, 2018), <https://www.hollywoodreporter.com/news/box-office-get-ready-hollywoods-shrinking-studio-system-1071457> (“Back in 2007, the six major studios released 150 titles, then midrange movies began falling off their slates. In 2017, they released 93.”).

<sup>19</sup> Tad Friend, *The Mogul of the Middle*, THE NEW YORKER (Jan. 11, 2017), <https://www.newyorker.com/magazine/2016/01/11/the-mogul-of-the-middle> (“The director Billy Ray traced the phenomenon [of franchises over adult dramas] to the economic collapse of 2008, and to the decline of the DVD market. ‘That’s when corporate timidity gave way to terror,’ he said. ‘Studio people actually said to me, ‘Don’t bring me anything that’s good, because I’ll be tempted to buy it, and I can’t.’”).

<sup>20</sup> Anne Thompson, *Fear of Netflix, Disney's Dominance, the Secret Success of MoviePass, and 5 More Things We Learned at CinemaCon*, INDIEWIRE (May 1, 2018), <https://www.indiewire.com/2018/05/10-things-cinemacon-hollywood-future-1201958718/> (“Theaters are begging for more movies in the \$50 million-\$100 million range to fill their screens, but the studios are increasingly disinterested. As the studios look for growth outside North America, they increasingly target movies overseas like domestic disappointments *Pacific Rim Uprising* and *Tomb Raider*. Finally, theaters look to the indies to fill that hole, among them Annapurna-MGM, STX, Global Road, A24, Entertainment Studios, and Neon.”).

<sup>21</sup> Motion Picture Association of America, THEATRICAL AND HOME ENTERTAINMENT MARKET ENVIRONMENT REPORT, 23-24 (hereinafter “THEME REPORT”)(2017)(Despite a 23% decrease in films produced by major studios and their subsidiaries from 2008 to 2017, the studios’ films represented over 80% of the domestic box office. Indeed, the top 25 films in 2017 accounted for 54% of the domestic box office, with the top five alone accounting for 19%).

<sup>22</sup> comScore, Inc.

## B. The Modern Multiplex Requires Ensured Variety of Content

The increase in multiplexes offers more screens to consumers, but not necessarily more variety.<sup>23</sup> Multiplex screens are increasingly taken up by longer runs on tentpole films. Studios press exhibitors to grant long runs on a number of screens for their blockbusters—a demand that has already forced small exhibitors to decline big movies because the theater cannot support the studio’s screen space demands based on the population it serves.<sup>24</sup> Without the prohibition on block booking, studios can push this trend to the extreme, requiring exhibitors to book multiple screens for multiple weeks on their entire slate—leaving no room for the variety consumers demand.<sup>25</sup>

Although it could be argued that the decreased variety in the theater would mean that the ostensibly missing content would migrate to home platforms, this argument has already proven to be wrong. Although some content may be purchased for exclusive runs on home entertainment platforms, filmmakers prioritize the myriad benefits of a theatrical release.<sup>26</sup> Small studios that choose a traditional distribution model also benefit from the legitimacy and box office receipts granted by a theatrical run.<sup>27</sup> Despite the plethora of options associated with in-home entertainment, the theatrical box office is the most vital and dependable source of revenue for studio content, and thus ripe for abuse if not carefully regulated.

## C. The Prohibition on Block Booking is Essential to the Effective Programming of High-Quality and Varied Programming Both in Theaters and in Ancillary Markets

The proliferation of options in the home has not diminished the primacy of the theatrical market for consumers and producers. In recent years, the demise of the lucrative DVD market amid the

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<sup>23</sup> There are currently approximately 4,679 complexes with 2 or more screens in the United States. comScore, Inc.

<sup>24</sup> Erich Schwartzel, *Disney Lays Down the Law for Theaters on ‘Star Wars: The Last Jedi,’* THE WALL STREET JOURNAL (Nov. 1, 2017), <https://www.wsj.com/articles/disney-lays-down-the-law-for-theaters-on-star-wars-the-last-jedi-1509528603> (“Few operators can afford to turn away a Disney windfall. But some independent theaters have decided against screening ‘Last Jedi’ when it is released, saying the company’s disproportionate share of ticket sales and four-week hold make little economic sense—especially in small towns . . . ‘There’s a finite number of moviegoers in my market, and I can service all of them in a couple of weeks,’ said Lee Akin, who operates a single-screen theater in Elkader, Iowa (population: 1,213).”).

<sup>25</sup> MARKETFORCE INFORMATION, MOVIE THEATERS: CONSUMER EXPERIENCES & COMPETITIVE BENCHMARKS, 12, 19 (Aug. 2018) (variety in titles is important to consumers).

<sup>26</sup> Ashley Rodriguez, *Netflix and Amazon are Pushing Out the Last Major Studios Still Seeking Smart Movies For Adults,* QUARTZ (Aug. 1, 2017), <https://qz.com/1043327/netflix-and-amazon-are-pushing-out-the-last-major-studios-still-seeking-smart-movies-like-detroit/> (studios that distribute theatrically have “an edge” over exclusively streaming platforms in purchasing the rights to quality midrange titles).

<sup>27</sup> Ashley Rodriguez, *US Cinema Chains Want Nothing to do With Netflix, but They Love Amazon,* QUARTZ (Apr. 3, 2017), <https://qz.com/947237/unlike-netflix-cinema-chains-really-want-to-work-with-amazon/> (Choosing a traditional distribution model “paid off” for Amazon. . . Amazon’s films released in its initial year, “including Kenneth Lonergan’s Oscar-winning drama *Manchester by the Sea*, collectively, have grossed more than \$90 million at the US box office . . .”).

rise of low-cost streaming has only increased the importance of the theatrical box office to distributors looking to justify the costs of a particular film.

Over the last decade and a half, the industry has seen domestic box office returns hold steady or increase, while revenues from in-home entertainment have declined by 50%. In 2004, the United States domestic box office brought in \$9.29 billion dollars while the home entertainment sector represented \$24.9 billion in revenue. Just 12 years later, in 2016, the domestic box office brought in \$11.37 billion while home entertainment revenues shrank to \$12.05 billion.<sup>28</sup> Put another way, even with the proliferation of streaming giants such as Netflix and Amazon, home entertainment spend has declined by 52% from its peak, while theatrical has grown 22% over the same period. This trend is continuing as consumers shift their habits to low-cost home options while an appetite for the big screen experience of a movie theater reached record levels this summer.<sup>29</sup> Last year, the theatrical box office accounted for a full 46% of combined theatrical and home entertainment consumer spending.<sup>30</sup> By 2017, low-cost, digital options represented the vast majority of the consumer spend in the home, while costlier physical home entertainment spending continued to decline, to almost half of what consumers spent in 2013.<sup>31</sup>

Success in an ancillary market is largely predicated on success in the theatrical market; the highest-grossing movies in theaters are also the highest-grossing movies in the home.<sup>32</sup> Therefore, if consumers wish to have a continued variety of high-quality content in the home at increasingly lower cost, a successful box office run is an increasingly critical requirement. As the trend in the home continues toward increasing quantity at ever-decreasing cost, the theatrical market is indispensable for studios looking to continue to invest in high-cost productions.

Furthermore, the streaming and movie theater markets are reliant on the same customers. Per a recent study by Ernst & Young:

**For every race and age demographic, average streaming hours per week is higher for respondents who visited a movie theatre 9 times or more than respondents who visited a movie theatre**

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<sup>28</sup> It is worth noting that the home entertainment number includes *all* forms of content, including television content and streaming platforms. The Digital Entertainment Group, MID-YEAR 2018 HOME ENTERTAINMENT REPORT (2018), [https://degonline.org/wp-content/uploads/2018/08/f\\_DEG-2Q18-Cover-Note-External-Grid.pdf](https://degonline.org/wp-content/uploads/2018/08/f_DEG-2Q18-Cover-Note-External-Grid.pdf)

<sup>29</sup> Jeremy Fuster, *2018 Summer Box Office Is Second-Best Ever – But It Got a Head Start*, THE WRAP (Sept. 4, 2018), <https://www.thewrap.com/summer-box-office-is-second-best-ever-but-theres-a-catch/>

<sup>30</sup> THEME REPORT, *supra* n.21 at 12.

<sup>31</sup> In 2013, theatrical box office spend was \$35.91 billion dollars globally, digital spend was \$12.30 billion and physical home entertainment spend was \$29.76 billion. In 2017 theatrical spend was \$40.58 billion, digital spend reached \$32.12 billion and physical spend reduced by nearly 50% to \$15.58 billion. *Id.*

<sup>32</sup> For example, in 2017 the top box office titles were also almost exclusively the top home video rentals. *See e.g.* THE NUMBERS, *Top-Selling Video Titles in the United States 2017* (2017), <https://www.the-numbers.com/home-market/packaged-media-sales/2017> (top movies in the home market for 2017); *2017 Domestic Grosses*, BOX OFFICE MOJO (2017), <https://www.boxofficemojo.com/yearly/chart/?yr=2017> (top domestic box office titles for 2017)

**only once or twice.** Moreover, respondents who visited a movie theatre in 2017 only once or twice reported an average of 8 hours of streaming per week versus 12 hours of streaming per week for those who visited a movie theatre 9 or more times.<sup>33</sup>

The Motion Picture Association of America’s (“MPAA”) 2017 Theatrical and Home Entertainment Market Environment Report similarly found that the most frequent moviegoers had a significantly higher share of ownership in home technology products when compared to the total adult population, with video-streaming device ownership particularly high.<sup>34</sup> Thus, the options in the home are decidedly not mutually exclusive with options in the theater.

D. Imminent Changes in Distribution Finance Model Could Heighten Antitrust Concerns as the Costs of Distribution Drop to Historic Levels

While the Department correctly identifies a number of changes to the motion picture industry in recent years, in many ways, the underlying economics of the movie distribution model have remained unchanged since the time of the Decrees. In the time of film, a distributor determined how many screens it should book for a particular feature based on a calculation that included the high cost of producing and shipping a film print, which could be as much as \$2,500 per run.<sup>35</sup> This high cost, combined with the promise of further technological capabilities, led the major studios to push for a transition from film projection to digital projection in the early 2000s.<sup>36</sup> Although studios stood to save upwards of \$1 billion a year by transitioning from film to digital delivery, this was only possible if exhibitors purchased equipment many times more expensive and far less durable than the film projectors they had used since the dawn of the industry.

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<sup>33</sup> ERNST & YOUNG, THE RELATIONSHIP BETWEEN MOVIE THEATRE ATTENDANCE AND STREAMING BEHAVIOR: SURVEY INSIGHTS (Apr., 2018), available at, <http://www.natonline.org/wp-content/uploads/2018/04/The-relationship-between-movie-theatre-attendance-and-streaming-behavior-4-26-18.pdf>. (emphasis added).

<sup>34</sup> THEME REPORT, *supra* n.21 at 22 (“More than three-quarters of all frequent moviegoers [79%] own at least four different types of key technology products, compared to 61 percent of the total adult population.”)

<sup>35</sup> Duane Marsteller, *Theater Owners Weigh Film Perfection, Conversion Costs*, USA TODAY (Feb. 22, 2013), <https://www.usatoday.com/story/life/movies/2013/02/22/digital-theater-movies/1940067/> (“It costs \$1,500 to \$2,500 to print and ship one copy of a 35-millimeter film, a figure that easily runs into the millions for a wide release.”)

<sup>36</sup> Helen Alexander & Rhys Blakely, *The Triumph of Digital Will Be the Death of Many Movies*, THE NEW REPUBLIC (Sept. 12, 2014) <https://newrepublic.com/article/119431/how-digital-cinema-took-over-35mm-film>. (“Digital formats began to displace film in earnest more than a decade ago and the charge was led by George Lucas. In 2002, Star Wars: Episode II-Attack of the Clones became the first major movie to be shot entirely on digital video, even though, back then, it had to be transferred on to 35mm film for most cinemas to show it. The producers of Attack of the Clones estimate that they spent \$16,000 on 220 hours of digital tape. If they had used the same amount of film, it would have cost them \$1.8 million”); Doreen Carvajal, *Nurturing Digital Cinema*, THE NEW YORK TIMES (May 23, 2005), <https://www.nytimes.com/2005/05/23/technology/nurturing-digital-cinema.html> (“But even so, this could be the rollout year for digital cinema. Some European countries are pressing forward with almost intergalactic ardor, subsidizing digital projector giveaway programs with the aim of nurturing home-grown movies that can flourish alongside Hollywood blockbusters . . . Theater owners who do not benefit from the same public bounty are moving more cautiously, waiting to see who will pay for digital technology that carries a price of more than \$100,000, or \$125,500, for a top-line projector.”)

Because of the lopsided economics involved, the studios and exhibitors entered into a series of agreements with third parties whereby the studios would subsidize the cost of the equipment by paying a “virtual print fee” (VPF) for each of their films to exhibitors through a third party.

The current VPF system has acted as an economic constraint to booking films on screens where there is marginal proven chance for profit. Studios must weigh the cost of the VPF when determining the number of screens they should book for a particular film. In many cases, studios—particularly smaller distributors—have judged the cost of distribution to be too high for some markets, causing those exhibitors to miss out on booking those films.

However, the VPF agreements were based on either a term of years or a recoupment schedule, and many have expired or are set to phase out within the next few years.<sup>37</sup> This change could potentially help increase product diversity for consumers by allowing some of the smaller distributors wider access to the market: As distribution costs decrease for smaller distributors, they may be more willing to book films in previously untapped markets, increasing diversity of product to consumers. It is critical that those exhibitors continue to have screens available for booking as more movies become available to them. However, a repeal on the prohibition on block booking could undermine this opportunity. With the end of the VPFs, the cost of distributing a film will decrease exponentially for all studios, ending the core economic considerations that distributors have relied on for generations. This, combined with the end of the prohibition on block booking, could unwind the core system of operations in the American movie industry. To do so, especially in the midst of such revolutionary change in the economic model of distribution, could have unintended consequences that could radically alter the quality and variety of films shown in our nation’s theaters and later in homes.

### **III. IMPOSING BLOCK BOOKING REQUIREMENTS ON EXHIBITORS WOULD HINDER THEIR ABILITY TO PROGRAM CONTENT BASED ON CONSUMER DEMAND**

As described earlier in this comment, a number of small studios have attempted to break into the theatrical market to focus on the films that the major studios have stopped making.<sup>38</sup> These films have won major awards, and have been crucial cultural touchstones for consumers.<sup>39</sup> Many of these films also reach diverse audiences, and have demonstrated the financial success of films

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<sup>37</sup> NATO recently conducted a member survey to gain a better understanding of the status of VPF deals. Nearly 200 members—representing approximately 16,700 screens—responded to the survey. 15% of respondents had already recouped, 11% will recoup within six months, and 17% will recoup between 6 months and one year. NATO, *President’s Report*, Vol. 19 (2 ed.) (Aug., 2018).

<sup>38</sup> See, *supra* Sections II(A), (C).

<sup>39</sup> For example, in 2015 *Spotlight* (Open Road) had a \$100 million worldwide gross and won Oscars for Best Picture and Best Original Screenplay; in 2016 *Moonlight* (A24) had a \$65 million worldwide gross and won Oscars for Best Picture, Best Supporting Actor, and Best Adapted Screenplay.

with diverse casts.<sup>40</sup> Indeed, even exclusively-streaming platforms such as Netflix are increasingly aware of the importance of a theatrical release on consumer awareness and recruitment of top-tier talent for their original content.<sup>41</sup> However, despite the importance of these films to consumers, they still only represent approximately 18% of the domestic box office,<sup>42</sup> leaving them vulnerable to becoming more limited or unavailable on exhibition screens if the block booking prohibition were removed.

Block booking an entire studio's film slate fails to account for consumer tastes in many different regions, and would put small town and limited screen/non-multiplex exhibitors and their guests at a significant disadvantage. Many exhibitors in small towns are unable to play most R-rated movies or movies with certain themes because their customers find those characteristics offensive.<sup>43</sup> Moreover, many of these theaters simply don't have the population to support the long runs already demanded by some distributors; despite the proliferation of multiplexes, 11% of the screens in the United States are from venues with fewer than five screens.<sup>44</sup> A system of long runs of entire slates would be disastrous to small town and/or limited screen exhibitors and their consumers, who may seek a wide variety of family-friendly and faith-based entertainment from distributors of all sizes, while avoiding other content entirely. For example, in 2017 a full 39% of titles released by major studios were rated R.<sup>45</sup> Exhibitors that are unable to show most R-rated films because of their consumers' tastes would be at a severe disadvantage should

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<sup>40</sup> See, e.g., Drew Harwell, *Diverse Movies Are a Huge Business. Why Doesn't Hollywood Make More?*, THE WASHINGTON POST (Dec. 15, 2015), [https://www.washingtonpost.com/business/economy/diverse-movies-are-a-huge-business-why-doesnt-hollywood-make-more/2015/12/15/ec002564-9774-11e5-b499-76cbec161973\\_story.html?noredirect=on&utm\\_term=.e2fdf382156e](https://www.washingtonpost.com/business/economy/diverse-movies-are-a-huge-business-why-doesnt-hollywood-make-more/2015/12/15/ec002564-9774-11e5-b499-76cbec161973_story.html?noredirect=on&utm_term=.e2fdf382156e) ("Some of [2015's] biggest surprises had diverse actors and small budgets but ended up dominating the silver screen"); see also Carrie Wittmer, *Movies with More Diverse Casts Also Make More Money at the Box Office, According to a Study*, BUSINESS INSIDER (June 21, 2017), <https://www.businessinsider.com/movies-with-diverse-casts-box-office-2017-6> (Describing a study by Creative Artists Agency that demonstrates "a diverse cast means a more diverse audience, which means more money at the box office.").

<sup>41</sup> See e.g., Dave Trumbore, *'I, Tonya' Opts for Traditional Distribution and Awards Eligibility over Netflix Deal*, COLLIDER (Sept. 11, 2017), <http://collider.com/i-tonya-netflix-oscars/#tiff-2017> (Margot Robbie turns down Netflix for *I, Tonya* distribution); Jackson McHenry, *Crazy Rich Asians Turned Down a Massive Netflix Offer to Make Sure It'd Be Seen in Theaters*, VULTURE (Aug. 1, 2018), <http://www.vulture.com/2018/08/crazy-rich-asians-turned-down-a-massive-netflix-offer.html> (*Crazy Rich Asians* writers turned down a massive Netflix offer to make sure it'd be seen in theaters); Brandon Katz, *In a Quest for Oscars, Netflix May Open Itself Up to More Theatrical Runs*, OBSERVER (Aug. 3, 2018), <https://observer.com/2018/08/netflix-original-movies-oscars-martin-scorsese-the-irishman-roma-22-july/> (Netflix looking to theatrical releases to lure top-tier talent).

<sup>42</sup> Figure based on grosses from all titled not released by Disney, Fox, Lionsgate, Paramount, Sony, Universal, Warner Bros. and their subsidiaries. comScore, Inc.

<sup>43</sup> "Callers [to the MPAA's Classification and Ratings Administration from the South in particular despise blasphemy . . . [callers from][t]he Midwest blanch[] at sex, especially in PG-13 movies. Residents of the coasts are concerned with violence." Erich Schwartzel, *These 11 People Watch Every Movie, Especially the Gross Bits*, THE WALL STREET JOURNAL (June 2, 2017), <https://www.wsj.com/articles/destroy-earth-just-dont-smoke-how-hollywood-decides-whats-acceptable-1496422644>

<sup>44</sup> In 2017 4,443 screens (11%) out of a total of 40,393 were from venues with fewer than five screens. THEME REPORT, *supra* n.21 at 27.

<sup>45</sup> Out of 145 titles released by Disney, Fox, Lionsgate, Paramount, Universal, Sony, and Warner Bros. in 2017, 57 titles (39%) were rated R. comScore, Inc.

studios demand block booking. A system that fails to account for varying local tastes means that consumers in these smaller markets are not able to attend the films they would like to see with members of their community. Many of these more rural areas also lack strong broadband service, further limiting their viewing options.<sup>46</sup>

The current system allows exhibitors the flexibility to program content based on their customers' demands. A repeal of the prohibition on block booking could render theaters unable to effectively program, force many exhibitors out of business, and leave consumers with fewer options for quality entertainment in the community. For example, exhibitors that operate in towns with shifting seasonal demographics will not be able to program based on their changing customers in a system where studio block booking is the norm; tourists in the summer months may want blockbusters while the locals during the off-season may only attend smaller, adult-oriented dramas. Both of these demographics are essential to the movie theater business, but neither would be effectively served if a theater had to accept an all-or-nothing deal in order to compete in the marketplace.

#### **IV. THE REPEAL OF THE PROHIBITION ON BLOCK BOOKING COULD REDUCE COMPETITION AND INCENTIVIZE ANTI-COMPETITIVE BEHAVIOR**

##### **A. The Abrupt Removal of the Block Booking Prohibition Could Create a Change in Custom that Could Prove Detrimental to the Industry and Ultimately to Consumers**

The history of motion picture production, distribution, and exhibition reveals the myriad opportunities and actual abuse of procompetitive distribution models even in the decades following the Decrees. For example, in *United States v. Loew's Inc.*, the court found that the Decrees remained important despite numerous “changes of significance in the motion picture industry” including the advent of VCRs and the “proliferation of cable television networks.”<sup>47</sup> Given “continued anti-competitive behavior by exhibitors and distributors . . .” the court declined to modify or exempt Warner Bros. from the provisions of the Decrees.<sup>48</sup> The court held:

It appears that some distributors and exhibitors have either formally or informally agreed to divide up the local markets. Not only does

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<sup>46</sup> “Fast, reliable internet service has become essential for everything from getting news to finding a job. But 24% of rural adults say access to high-speed Internet is a major problem in their local community . . . . An additional 34% of rural residents see this as a minor problem, meaning that roughly six-in-ten rural Americans (58%) believe access to high speed Internet is a problem in their area.” Monica Anderson, *About a Quarter of Rural Americans Say Access to High-Speed Internet is a Major Problem*, Fact Tank, Sept. 10, 2018, <http://www.pewresearch.org/fact-tank/2018/09/10/about-a-quarter-of-rural-americans-say-access-to-high-speed-internet-is-a-major-problem/>

<sup>47</sup> 705 F. Supp. 878, 890 (S.D.N.Y. 1988)

<sup>48</sup> *Id.*

this kind of behavior fly in the face of the requirement of all the consent judgments that films be licensed theatre by theatre, solely upon the merits and without discrimination, but it raises troubling and serious questions as to the vigor with which the antitrust laws are being enforced. While it would be inappropriate to speculate on the legal consequences of facts not before the court, **we find this apparent climate of noncompliance with the Paramount decrees and with the antitrust laws to be fraught with serious problems. We cannot allow that climate to go unchecked and unsupervised, and we can see no reason why Warner's participation in the joint venture will be unduly harmed by such supervision.**<sup>49</sup>

There is no question that the Decrees changed the infrastructure and marketing practices of the motion picture industry and have continued to do so through today. The Decrees quelled many of the earlier abuses and created a much freer market that enabled competition by independent producers, availability of more diversified product, competitive opportunities for independent exhibitors, and competitive marketing to consumers. However, as described by the *Loew's* court, the studio distribution and exhibition business models reflect how such abusive business practices could easily re-emerge absent sufficient protections as those afforded by the Decrees.<sup>50</sup>

The movie distribution and exhibition system has developed around the strictures of the Decrees. In an industry with so much history and a number of family-owned businesses, many decision-makers in distribution and exhibition have worked for multiple companies and bring sometimes generations of family industry knowledge with them. Indeed, despite not being bound by the Decrees, major studios such as Disney and Lionsgate tend to generally operate within the bounds of the Decrees.<sup>51</sup> Thus, the Decrees act as a set of customs that are largely respected by distribution and exhibition and which continue to serve the procompetitive interests mandated by both statutory and judicial precedence.

This review comes as new players are entering the market, many without historic ties to the industry.<sup>52</sup> Currently, new entrants are generally honoring the distribution models as determined

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<sup>49</sup> *Id.* at 890-891 (emphasis added).

<sup>50</sup> To a limited extent, even without the Decrees, existing laws could be violated if such restricted behaviors were repeated. However, the existence of the Decrees have and will continue to act as a deterrent to those willing to engage in anticompetitive behaviors. Therefore, to the extent the Decrees are to be modified, we urge the Department to ensure that any such efforts be narrowly tailored to maintain the procompetitive benefits of the Decrees.

<sup>51</sup> However, see *supra* n.24 and Section IV(B), *infra*.

<sup>52</sup> For example, Netflix and Amazon have both reportedly shown interest in purchasing exhibition chain Landmark Theaters, likely with very different distribution models. See Johnny Lieu, *Amazon is Reportedly Looking to Buy Up a Cinema Chain, to Expand Its Growing Footprint in Film*, MASHABLE (Aug. 16, 2018,

and developed by the limitations in the Decrees. However, abandoning the Decrees could result in an era of “experimentation” that could lead to decreased product and potentially the end of many smaller exhibitors and distributors. As described above, the combination of the expiration of the VPF system with a repeal in the prohibition on block booking alone could lead to fundamental changes to America’s movie production, distribution, and exhibition system with consequences that could prove disastrous.

#### B. Removing the Prohibition on Block Booking Would Amplify Anticompetitive Pricing Effects

Block booking could threaten exhibitors’ ability to experiment with business models that take advantage of changes in technology and consumer habits. The Decrees prohibited distributors from requiring “fixed minimum admission prices” for the licensing of their films by exhibitors.<sup>53</sup> The goal of this provision was “to open the market to independent producers and distributors, to allow exhibitors to select which movies they would show, and to remove artificial constraints on ticket pricing.”<sup>54</sup>

For some time following the Decrees, exhibitors regularly used price variation for movie type, day of the week, and even seat location.<sup>55</sup> However, since at least the 1970’s, exhibitors have offered a standardized ticket pricing model, regardless of the cost, quality of the content, or the number of screens licensed.<sup>56</sup> Absent exceptions for matinees, some youth and/or senior discounts, and markups for specialized screens or services, customers pay the same price

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<https://mashable.com/article/amazon-cinema-landmark-theatres/#48Ka.gvkoQl> (Amazon potentially looking to break into exhibition to add to its new distribution presence, but “[a]lthough Amazon is also a disruptor, it sticks to convention when it comes to distribution. It runs movies in cinemas for months before they sit on Prime Video, and is public about ensuring its films screen in theaters.”); *compare with*, Lizzie Plausic, *Netflix has Reportedly Considered Buying Theaters to Screen Its Movies*, THE VERGE, Apr. 19, 2018, <https://www.theverge.com/2018/4/19/17258114/netflix-theaters-landmark-mark-cuban-buying-screenings-oscar-cannes> (Netflix also reportedly considering purchasing an exhibition chain to increase awards eligibility: “Owning a theater or theater chain would make it easier for Netflix to qualify for other Hollywood awards like the Oscars, which also require that films see a theatrical release in order to be eligible. Although Netflix films like *Beasts of No Nation* and *Mudbound* were screened in a limited number of theaters, the streaming service has stuck to a day-and-date structure, meaning those films were available to watch simultaneously in theaters and on Netflix.”)

<sup>53</sup> *Paramount* 334 U.S. at 141

<sup>54</sup> Barak Y. Orbach, *Antitrust and Pricing in the Motion Picture Industry*, 21 YALE J. ON REG. 317, 342 (2004)(citation omitted)

<sup>55</sup> B Barak Y. Orbach & Liran Einav, *Uniform Prices for Differentiated Goods: The Case of the Movie-Theater Industry*, 27 INT’L REV. L. & ECON. 129, 143 (2007) (“[T]hroughout the 1950s and 1960s there was a clear distinction between pricing of regular and event movies. Exhibitors also maintained price variation between weekdays and weekends and among different types of seats.”).

<sup>56</sup> Harrison J. Reynolds, *Introducing Price Competition at the Box Office*, 20 UCLA ENT. L. REV. 11, 14 (2013) (“Admissions tickets for movies are priced uniformly, without regard for the distinctive characteristics of particular films. This practice first appeared in the early 1970s, and is popularly believed to have begun with the regular admission prices charged nationwide for *The Godfather* in 1972 [in all likelihood due to pressure from the producer–distributor Paramount]. Eventually, uniform pricing across all movies became the norm, and then the rule.”) (internal citations omitted).

regardless of the movie they pick or when they choose to watch the movie. Much of the uniformity in price can be attributed to the distributors' use of per capita requirements, which set a floor on pricing per customer for licensing fee purposes.<sup>57</sup>

Changes in technology offer exhibitors new ways to innovate to reach their customers. Customer loyalty programs combined with data analytic tools can help exhibitors understand their frequent guests.<sup>58</sup> This data can in turn help exhibitors make targeted marketing and programming choices based on their consumers' preferences.<sup>59</sup> Third-party apps can allow groups of friends to choose a movie, theater location, showtime, and even purchase tickets from their phones.<sup>60</sup> Some apps also use sophisticated economic models to offer options in variable pricing.<sup>61</sup> Testing of these models has shown promise, with box office and attendance increases of up to 15%.<sup>62</sup> Despite evidence of successful test cases, U.S. exhibitors have not adopted widespread variable pricing.<sup>63</sup>

Exhibitors wishing to embrace new technologies to grow their box office must often contend with their studio partners, who have disfavored variable pricing in the modern era. Attempts by exhibitors to offer alternate models to consumers have reportedly been met with discouragement, outright threats,<sup>64</sup> or financial penalties in the form of per capita charges by distributors.<sup>65</sup> Because major studios license the vast majority of the films each year, exhibitors may choose not

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<sup>57</sup> *Id.* at 323 (“Distributors have maintained price control without holding on to tied economic interests, and the result is anticompetitive resale price maintenance.”)

<sup>58</sup> <https://www.jackroe.com/loyalty-membership-gift-cards/> (Loyalty programs . . . increase the frequency of visits by existing customers, they also turn those customers into advocates for your cinema); <https://loyalty360.org/content-gallery/daily-news/humanizing-customer-data-and-cinema-loyalty-progra> (“the key opportunity for sustainable and profitable differentiation is for exhibitors to know their guests and treat them as individuals in a way that sees them enthusiastically choose their cinemas over the competition, return more frequently and spend more when they visit. Loyalty programs are the foundation of this.”)

<sup>59</sup> *Id.*

<sup>60</sup> <https://www.atomtickets.com/about> (“Atom’s user-friendly and socially driven interface allows movie lovers to search for films instantly, invite friends, buy tickets, pre-order concessions and enjoy a VIP experience at the theater. The platform’s innovative marketing solutions and young, diverse user-base help studios, exhibitors and brands reach their target audience and maximize revenue opportunities.”)

<sup>61</sup> <https://smart-pricer.com/cinema/>

<sup>62</sup> *Id.*

<sup>63</sup> J. Sperling Reich, *Some Advice For Regal Cinemas On Dynamic Movie Ticket Pricing*, CELLULOIDJUNKIE (Nov. 1, 2017), <https://celluloidjunkie.com/2017/11/01/advice-regal-cinemas-dynamic-movie-ticket-pricing/> (Regal, under previous ownership, announced a “ticket pricing test” for early 2018 and stressed that the test would have to “provide a clear economic benefit . . . to our studio partners.”)

<sup>64</sup> Orbach & Einav, *supra* n.55, at 150 (noting that distributors “enforce uniform pricing by refusing to deal with exhibitors that wish to switch to variable pricing”); Adam Dawtrey, *EasyCinema fails to woo U.S. majors*, VARIETY (May 9, 2003), <https://variety.com/2003/film/news/easycinema-fails-to-woo-u-s-majors-1117885928/> (founder of company with variable pricing model alleges major studios refused to give him content).

<sup>65</sup> See, e.g. Jill Goldsmith, *AMC Tempts Auds with Multi-Pic Card*, DAILY VARIETY (June 11, 2001), p. 28 (describing a discount program of a major theater circuit and quoting the distribution chief of DreamWorks saying that they could not tell exhibitors what to charge but could include per-capita requirements in the rental contracts); Andrew Hindes, *Multiplex Showdown in Desert*, VARIETY (Mar. 24, 1997) (“In the event that one or both [of the competing] exhibitors decides to slash admission prices, distrib[utors] have the option of selling pictures on a ‘per capita’ basis, collecting a fixed amount per patron.”).

to unilaterally adopt variable pricing, out of fear distributors will cease providing content.<sup>66</sup> Major distributors include additional terms in their agreements that stifle innovation, including bans on screen splitting and demands for a minimum exhibition period, regardless of consumer demand.<sup>67</sup>

Independent distributors hoping to entice moviegoers with discounts or other pricing incentives have had to partner with third parties, a less desirable model than partnering directly with exhibitors, given instability in third-party business models,<sup>68</sup> problematic consumer data use,<sup>69</sup> and failure to include key partners in discussions.<sup>70</sup>

The combination of loyalty data, ticketing apps, and alternate pricing models could allow exhibitors to innovate in order to grow their customer base.<sup>71</sup> Particularly, as the costs of distribution drop with the expiration of the VPFs, independent studios could afford wider releases on more of their films. These distributors could partner with exhibitors to offer price incentives to help their films compete against tentpole releases and their corresponding behemoth marketing budgets. This could help more midrange films succeed, and could contribute to growth in the sector based on demonstrated consumer demand. As described above, the success of these films in the theater would likely translate to further success in ancillary markets.

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<sup>66</sup> Reynolds, *supra* n.56 at 44-45, (“Exhibitors and distributors are playing a game of chicken, and distributors are consistently winning. . . Each exhibitor is afraid to independently switch to variable pricing, because it will lose distributor business and will accordingly be unable to compete with other exhibitors who stick with uniform pricing and thus maintain access to more films.”).

<sup>67</sup> Krzysztof Wozniak, *Vertical Restraints in the Movie Exhibition Industry*, 7-8 (2014), available at <http://econweb.umd.edu/~sweeting/wozniak.pdf>.

<sup>68</sup> Yohana Desta, *Enjoy MoviePass While You Can, Folks*, VANITY FAIR (May 10, 2018), <https://www.vanityfair.com/hollywood/2018/05/moviepass-sec-filing-future> (“In the last few months, MoviePass has . . . burned through so much money that its future looks unstable at best. The question plaguing the company now: how much longer can it last?”); Ashley Rodriguez, *MoviePass is dying. Is it worth switching to its biggest rival?*, QUARTZ (Aug. 4, 2018), <https://qz.com/1344064/moviepass-is-dying-is-it-worth-switching-to-its-biggest-rival/> (“[R]ight now, [subscription app Sinemia] is clunky and confusing, and the fees it saddles subscribers with quickly add up.”)

<sup>69</sup> David Z. Morris, *MoviePass Wants to Gather a Whole Lot of Data About Its Users*, FORTUNE (Mar. 10, 2018), <http://fortune.com/2018/03/10/moviepass-data-gathering/> (Movie subscription service MoviePass CEO described the company’s use of data: “[W]e get an enormous amount of information. Since we mail you the card, we know your home address . . . we know the makeup of that household, the kids, the age groups, the income. It’s all based on where you live. It’s not that we ask that. You can extrapolate that. Then . . . [b]ecause you are being tracked in your GPS by the phone . . . we watch how you drive from home to the movies. We watch where you go afterwards, and so we know the movies you watch. We know all about you. We don’t sell that data. What we do is we use that data to market film.”)

<sup>70</sup> Pamela McClintock, *Theater Chief Questions Whether Subscription Plans Like MoviePass Are Sustainable*, THE HOLLYWOOD REPORTER (Apr. 24, 2018), <https://www.hollywoodreporter.com/news/theater-chief-questions-subscription-plans-like-moviepass-are-sustainable-1105474>; Bret Lang, *The Great Disruptor: MoviePass Upends the Movie Business, but Can It Survive?*, VARIETY (2018), <https://variety.com/2018/film/features/moviepass-movie-business-studios-amc-1202754312/> (one subscription service described by studio distribution executive as “a cancer on the industry” in part based on failure to work with industry players).

<sup>71</sup> See, e.g., MARKETFORCE, *supra* n.25 at 12 (vast majority of consumers surveyed would attend movie theaters more frequently if there were more pricing incentives).

However, if the prohibition on block booking is repealed, large distributors could prevent outright the scale of release needed by independent distributors and exhibitors to prove that variable price options can effectively grow the box office. Without the ability to guarantee a wide release, or even a tailored platform release, independent studios will not have the screens they require for midrange movie success, to the detriment of consumers.

The current uniformity of pricing suggests that *more* intervention is needed to enforce the policy concerns of the *Paramount* Court. The per capita requirements are not unlawful on their own.<sup>72</sup> However, the film industry must be viewed in context.<sup>73</sup> In *Paramount*, the Court found that the studio's actions on their own were facially lawful but nonetheless held that the facts of the industry and the uniformity of pricing implied that the studios were working in concert.<sup>74</sup> The current uniformity of pricing similarly suggests that the studios have been able achieve the same result (fixed minimum prices) indirectly as they had previously sought directly. This inference is bolstered by the pattern of publicly sharing the intention to enforce minimum pricing demands in connection with exhibitors' attempts to innovate.

Per capitas have the same effect of discouraging discounting and price competition as the direct price fixing had at the time of the Decrees.<sup>75</sup> The current pricing model does not survive rational scrutiny,<sup>76</sup> and has hampered exhibitors' ability to use price incentives to meet consumer demand. If the prohibition on block booking were removed, distributors could take advantage of the facial lawfulness of the per capita requirements and the ability to book out an entire slate on multiple screens to quash attempts by exhibitors to book midrange films on wide release with variable pricing incentives. Consumers in turn will get less product at higher prices.

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<sup>72</sup> *Gen. Cinema Corp. v. Buena Vista Distrib.*, 681 F.2d 594 (9th Cir. 1982)

<sup>73</sup> Orbach & Einav, *supra* n.55 at fn.7 (“Pursuant to *Paramount*, distributors introduced ‘per-capita requirements’ in licensing agreements that set minimum amounts paid to a distributor for any patron who watches the licensed movie. Practically, the per-capita requirements affect box-office pricing, but they were upheld by the Ninth Circuit.”)

<sup>74</sup> *Paramount*, 334 U.S. at 142 (determining by inference that a horizontal agreement existed between defendants based on the “pattern of price fixing disclosed in the record”); see also *United States v. Paramount Pictures, Inc.*, 334 F. Supp. 323, 336 (S.D.N.Y. 1946) (“The whole system presupposed a fixing of prices by all parties concerned in all competitive areas”); Gil, *supra* n.8 at 111-12 (“The implication of this logic is that absent an agreement between all defendants to set a minimum admission price, one or more of the defendants would have lowered its admission price, thereby attracting more consumers and forcing price competition.”).

<sup>75</sup> See, e.g., *Reynolds*, *supra* n.56 at 5 (in understanding the current uniformity at the box office, “all seems seem to point towards” price fixing by the distributors.)

<sup>76</sup> *Id.* (uniform price structure creates market inefficiencies that harm consumers); see also Orbach & Einav *supra* n.55 (discussing the limitations on uniform pricing and suggesting models for variable pricing).

### C. Removal of the Decrees Would Result in Widespread Litigation to Address Unresolved Legal Issues

Though there is a strong line of cases holding the block booking of films to be illegal per se, the existing antitrust laws, including the precedent of *United States v. Paramount* and its progeny, are not sufficient on their own to protect competition in the face of potentially rapid change following any modification or repeal of the Decrees. Specifically, courts have not taken a consistent analytical approach to tying and bundling cases involving intellectual property, leaving room for anticompetitive actions and effects before any court can definitively hold a behavior anticompetitive. The inconsistencies of interpretation could leave independent distributors and many exhibitors vulnerable to anticompetitive harms before the courts could provide clarity.

Following the *Paramount* decision, the Supreme Court in *United States v. Loew's Inc.* held that the block booking of films is illegal per se.<sup>77</sup> The Court reasoned that given the facts commonly at play in a block booking arrangement, that the contracts “both by their ‘inherent nature’ and by their ‘effect’ injuriously restrained trade.”<sup>78</sup> The Court held “[e]nforced block booking of films is a vice in both the motion picture and television industries, and that the sin is more serious (in dollar amount) in one than the other does not expiate the guilt for either.”<sup>79</sup>

Courts have held that the per se standard applies when the facts are parallel to the block booking system described in *Paramount* and *Loew's*.<sup>80,81</sup> For example, in 1999, the U.S. Court of Appeals for the Eleventh Circuit applied the per se rule to a package license for television programming because the package at issue could not be distinguished from the block booking that the Supreme Court declared to be illegal per se in *Loew's*.<sup>82</sup> Other courts have similarly concluded that a per se standard applies when the facts mirror those of the *Paramount* case.<sup>83</sup>

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<sup>77</sup> *United States v. Loew's, Inc.*, 371 U.S. 38, 49-50 (1962).

<sup>78</sup> *Id.* at 48-49 (agreeing with the District Court judge that each copyrighted film block booked by appellants for television use “was in itself a unique product”; that feature films “varied in theme, in artistic performance, in stars, in audience appeal, etc.,” and were not fungible; and that since each defendant by reason of its copyright had a “monopolistic” position as to each tying product, “sufficient economic power” to impose an appreciable restraint on free competition in the tied product was present.)

<sup>79</sup> *Id.* at 50.

<sup>80</sup> In *Loew's*, the Court confirmed the holding in *Paramount* that block booking was per se illegal. 371 U.S. at 49-50. The final judgment went beyond the prohibition in *Paramount* by requiring the defendant to offer the films individually at the outset of the negotiations and prohibiting price differentials between individual prices and package prices that could not be cost justified. *Id.*

<sup>81</sup> *Six West Retail Acquisition, Inc. v. Sony Theatre Mgmt. Corp.*, 2004 U.S. Dist. LEXIS 5411, \*15 (S.D.N.Y. Mar. 31, 2014) (block booking of the type described by the *Paramount* court is per se illegal).

<sup>82</sup> *MCA Television Ltd. v. Pub. Interest Corp.*, 171 F.3d 1265, 1277-78 (11th Cir. 1999) (citing *Loew's*, 371 U.S. at 50).

<sup>83</sup> See, e.g., *Six West Retail Acquisition, Inc. v. Sony Theatre Mgmt. Corp.*, 2004 U.S. Dist. LEXIS 5411, \*15 (S.D.N.Y. Mar. 31, 2014) (block booking of the type described by the *Paramount* court is per se illegal).

However, in recent years, courts and the Department have demonstrated a preference for a rule of reason analysis in intellectual property bundling cases.<sup>84</sup> In *Illinois Tool Works Inc. v. Independent Ink, Inc.*, the Supreme Court held that ownership of a patent alone would no longer be per se evidence of market power.<sup>85</sup> Although courts acknowledge that the per se standard may still apply in certain cases,<sup>86</sup> they may be more likely to choose to apply a market power analysis where the facts are similar but not identical to those described in *Paramount*.<sup>87</sup>

Should the Department remove the prohibition on block booking, distributors could take advantage of the change in the status quo to develop booking obligations that diverge only superficially from those in the *Paramount* case and its progeny. If challenged, distributors could argue that the longstanding per se prohibition should not apply, and could initiate costly and lengthy court proceedings. This could give rise to widespread litigation and forum shopping, as parties attempt to redefine the laws and practices that have governed the industry for seventy years. Although the laws may be able to prohibit all forms of block booking eventually, many small studios, exhibitors, and consumers would suffer from the uncertainties and expenses of the anti-competitive landscape created by such ambiguities.

## V. CONCLUSION

Abandoning the prohibition on block booking will likely reduce competition and incentivize anti-competitive behavior. As demonstrated above, the current distribution model depends on a small number of studios with significant bargaining power. These studios are producing increasingly expensive content for global audiences, and demanding longer runs on more screens from exhibitors, as the overall financial success of a movie is increasingly dependent on theatrical box office. At the same time, major studios are also decreasing their slates and

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<sup>84</sup> See, *United States v. Microsoft*, 253 F.3d at 95. (In deciding a tying patent misuse claim, the U.S. Court of Appeals for the Federal Circuit rejected a per se approach and applied tying case law to find that a package license combining alleged “essential” with “nonessential” patents did not constitute patent misuse because there was no separate demand for the “nonessential” patents, and, thus, no separate product market in which competition could have been foreclosed. *U.S. Philips Corp. v. Int’l Trade Comm’n*, 424 F.3d 1179, 1193-97 (Fed. Cir. 2005). The court rejected a per se approach “[i]n light of the efficiencies of package patent licensing and the important differences between product-to-patent tying arrangements and arrangements involving group licensing of patents . . . .” *Id.* at 1193; see also U.S. DEP’T OF JUSTICE & FEDERAL TRADE COMM’N, *Antitrust Guidelines for the Licensing of Intellectual Property* § 5.3 & n.34 (1995), available at <http://www.usdoj.gov/atr/public/guidelines/0558.pdf>.

<sup>85</sup> *Ill. Tool Works Inc. v. Indep. Ink, Inc.*, 547 U.S. 28, 45-46 (2006) (“Congress, the antitrust enforcement agencies, and most economists have all reached the conclusion that a patent does not necessarily confer market power upon the patentee. Today, we reach the same conclusion.”); see also *Mediacom Commc’ns Corp. v. Sinclair Broad. Grp.*, 460 F. Supp. 2d 1012, 1027-28 (S.D. Iowa 2006) (extending the *Independent Ink* holding to copyrights)

<sup>86</sup> *Id.* at 14–15. (“[C]ertain tying arrangements pose an unacceptable risk of stifling competition and therefore are unreasonable ‘per se’ due to the ‘substantial potential for impact on competition’ that occurs when a seller’s dominant position in a tying product market is used as leverage to force the sale of tied products.”)

<sup>87</sup> *Ill. Tool Works Inc. v. Indep. Ink, Inc.*, 547 U.S. 28, 45-46 (2006) (“Congress, the antitrust enforcement agencies, and most economists have all reached the conclusion that a patent does not necessarily confer market power upon the patentee. Today, we reach the same conclusion.”); see also *Mediacom Commc’ns Corp. v. Sinclair Broad. Grp.*, 460 F. Supp. 2d 1012, 1027-28 (S.D. Iowa 2006) (applying *Independent Ink* to copyright).

abandoning production of many small and midrange titles that American audiences demand, leaving independent distributors to produce the content studios no longer make.

Exhibitors require a variety of content in order to appeal to the varied tastes of their consumers. The prohibition on block booking has allowed exhibitors to use their screens to program both major studio content and other, more targeted fare. This in turn ensures the continued availability of high-quality and varied content in the home that consumers demand, since (1) success in the home is often directly correlated with success in the box office, and (2) the trend toward low-cost streaming options in the home emphasize the financial importance of box office success.

If distributors are permitted to block book, they could demand exhibitors book an entire slate on multiple screens, leaving little room for the independent and smaller distributors to finance and distribute films that consumers demand. The risks of “overbooking” a film on a multiplicity of screens are exacerbated with digital distribution, as the historic high costs associated with shipping film prints are set to expire entirely in the next few years, reducing the cost of film distribution to close to zero.

Block booking could also stifle exhibitors’ nascent attempts to offer innovative pricing incentives. Without the prohibition, major studios may demand longer runs on more screens, both growing their leverage over exhibitors and diminishing the ability of smaller studios to develop consumer-driven pricing incentives in partnership with exhibitors.

Finally, distributors could take advantage of ambiguities in the laws governing tying and bundling of intellectual property rights, resulting expensive and lengthy litigation before clarity is provided by the courts. Many smaller exhibitors and distributors could go out of business in that time, removing vital content and access to consumers.

Accordingly, NATO urges the Department to maintain the protections provided by the Decrees in the prohibition on block booking, as that prohibition continues to support pro-competitive practices.