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### Organizational dynamics in social networks : contracts and reputations in the film industry

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## Chapter 6:

### Conclusion

#### *Findings and theoretical implications*

The overall aim of this thesis is to gain insight in the organizational dynamics of project-based industries. Project-based industries are organized around single purpose project-based organizations (PBOs) that are disbanded after completion of the project for which it was specifically set up (DeFillippi & Arthur, 1998). Individuals in these industries, often freelance professionals, are continuously searching for new projects to join, or other individuals to join the projects they have set up themselves. Project-based industries, in other words, are characterized by continuously shifting temporary alliances, of which the industry can be regarded as the social network, the professionals that are active in that industry as the nodes of this network, and the project collaborations as the ties connecting these nodes. Looking at project-based industries in terms of social networks of nodes connected by ties, in turn, allows one to study its structure and dynamics by applying the theories and methods developed in the academic field of social networks. The empirical setting of this thesis is the project-based Dutch film industry in which four studies were conducted.

Chapter two focused on the contracts and rewards that govern the relationships in the film industry. It showed that film producers and others professionals in the film industry have a preference to serially collaborate with the same individuals in PBOs that are contractually isolated in the narrow legal sense. These so-called latent organizations (Starkey et al., 2000) are governed by long-term implicit or relational contracts (MacNeil, 1980; Baker et al., 1997, 2002) that lower transaction costs (Williamson, 1981). In addition, relational contracts in latent organizations create similar organizational benefits to those of labor contracts in normal organizations such as flexibility of employees in the tasks they have to

perform, and flexibility in the kind and timing of rewards. Members of latent organizations are sometimes willing to work under suboptimal conditions in a current project as compensation for having enjoyed certain benefits in a past project or because they expect to be compensated in a future project. The former is can be referred to as the 'shadow of the past' and the latter as the 'shadow of the future' (Poppo, Zhou & Ryu, 2008). Finally, latent organizations allow for quasi-internal labor markets to take root in which individuals benefit from a certain degree of job stability or preferential access to new projects and increased chances of making 'internal' promotions.

The findings of chapter two have several implications. It has been argued that formal or explicit contracts are costly alternatives for relational exchanges (Gulati, 1995b). Others posit that exchanges between organizations are primarily built on long-term explicit contracts and complemented by implicit or relational contracts (Poppo & Zenger, 2002). In latent organizations, however, it is the other way around in the sense that the explicit or short-term transactional contracts in the PBO largely complement the implicit or long-term relational contracts of the underlying latent organization. In other words, transactional contracts can in certain cases be considered to derive from relational contracts. This, in turn, has implications for career strategies. Depending on their career stage freelancers need to balance strong and weak social network ties. Strong ties within latent organizations provide more stable work relationships, trust and efficiency. In addition, freelancers who precisely because of their freelance status face difficulties in making career steps (O'Mahoney & Bechky, 2006), *ceteris paribus*, are more likely to make a promotion within the quasi-internal labor market of the latent organization. Weak ties, on the other hand, increase the number of information channels that allow freelancers to hear about work opportunities or new projects from many different sources, and make them less dependent on one or a small number of sources.

Chapter three was concerned with modeling the evolution of social networks of film producers, directors and scriptwriters by estimating the effects of certain types of reputation on tie or alliance formation. Before strong ties among members of latent organizations can take shape – the subject of the former chapter – initial

ties need to be formed first. This dynamic process was studied by statistically modeling the evolution of the social network focusing particularly on the effects of individual actor characteristics on the formation and dissolution of collaboration ties (Snijders et al., 2005, 2006, 2009). The main characteristics of interest were reputations derived from the performance of films in which individuals participated in the past that are important carriers of information that aid in determining the value or quality of potential alliance partners (Podolny, 1993, 1994). The findings indicated that individuals with a high artistic reputation, based on favorable film critics' reviews, are more likely to form new collaboration ties. Artistic reputations, and the critics' reviews on which they are based, are therefore important drivers of the evolution of the industry network. No similar tendency was found with respect to commercial reputation based on return on investment of past films. Finally, there was no evidence for status-based homophily selection or a disproportional tendency of individuals with similar reputations to form ties.

Thus, the outcomes of this study in the setting of the Dutch film industry do not support theories of status-based homophily selection stating that individuals (Festinger, 1954) or organizations of similar status tend to form ties or alliances (Podolny, 1993, 1994). Podolny argues that in highly uncertain markets, such as the film industry, organizations tend to form long-term exchange relations. With respect to individuals the study of latent organizations in chapter two confirmed this argument of Podolny. In addition, he posits that in uncertain markets, there is a tendency to form exchange relations with others of similar status. The results in this thesis, however, provide no strong empirical evidence to support this. Finally, he argues that status derives not only from an individual's own reputation but also from the status of its exchange partners. Yet no evidence for status-based homophily selection based on reputational status was found, even when taking spillover effects into account. The results of the current study do show that there is a strong tendency towards local clustering, in other words, alliance formation between individuals that are close to each other in the network.

An implication of these findings is that in explaining tie or alliance formation, there is a need, first, to distinguish between different *forms of status*, namely network position, non-merit based status such as gender and reputational status

based on past performance, and second to distinguish between different *types of reputations*, namely market, expert and peer. Both the form of status and the type of reputation may play a role in explaining alliance formation. Since no empirical support was found for status-based homophily selection based on the external signals of commercial or artistic reputation, while in line with Gulati's (1995a) earlier findings, empirical support was found for network position or closeness predicting tie formation, it might be that *if* there is a tendency towards status-based homophily selection in alliance formation, it might be better explained by similarity of peer reputation based on internal industry signals.

In chapter four the value was analyzed of certain types of reputation – market, expert, and peer – in obtaining investment capital for films from different types of investors. It should be noted that expert reputation is a different name for artistic reputation as used in the previous chapter. The finding in the former chapter that expert – or artistic – reputations are a dominant driver of the collaboration network of film professionals may be related to the relative value of expert reputations in obtaining investment for films. The results of this study show that certain types of reputation are more valuable if they match the dominant type of selectors in the selection system (Gemser et al., 2008). In the Dutch film industry, public broadcasters – including the related CoBo and Stifo Funds – are the most important film investor in terms of investment share. More specific, we found that *expert reputations*, derived from favorable critics' reviews of past films, of both producers and directors, are strong predictors for obtaining investment capital from public broadcasters that can be characterized as *expert selectors*. The higher value of expert/artistic reputation in obtaining investment capital may be the underlying reason why the evolution of the industry network is to a large extent driven by individuals with expert/artistic reputations.

These findings of the effects of matching types of reputations and selection systems have implications for competition processes and institutional theory. As opposed to distinguishing between different *sources* of isomorphism that explain why organizations behave similarly (DiMaggio & Powell, 1983), this study distinguished between different *stages* in the competitive process that, in turn, may have different sources of isomorphism. Competition can be viewed as a staged

process where different types of reputation or status determine success in different stages of the competitive process. The evaluation standards of start-up capital providers in the first stage of the competitive process shape the competitive environment in the second stage where products, in this case films, vie for the attention of end-users or consumers. Moreover, the evaluation standards of these end-users may be different from those of investors. In order to be successful in each stage may require having different types of reputations. The larger the number of stages in the competitive process and the larger the differences in evaluation standards in each of these stages, the more important it becomes to balance different types of reputations in order to be successful in the overall competitive process.

These findings also have implications for policies to support the film industry. A tendency of public broadcasters to invest in film projects by filmmakers with high expert, as opposed to market, reputations creates an oversupply of artistic films in the end-user or consumer market most of which will not be commercially successful. In other words, instead of film critics' reviews being influencers or predictors of success at the box-office (Eliashberg & Shugan, 1997; Gemser et al., 2007) it seems that they are influencers or predictors of success in obtaining investment capital for future film projects. In addition, when dominant selectors in the investment phase have a propensity to value expert or artistic reputations this might also create an incentive for filmmakers to develop more artistic film proposals since this will increase the chance of receiving investment capital. If there is an additional policy objective to support the production of mainstream films there is a need to create a selection system at the investment phase in which market selectors are dominant. This might imply the introduction of two separate investment models for art-house and mainstream films. This could be something to explore in further research.

In addition, because of the high value of expert reputation in receiving investment capital for films it might be that, in general, professionals in the Dutch film industry make and value artistic films more than they do mainstream films. In turn, the peer jury that nominates and hands out Gouden Kalf awards at the Dutch Film Festival may be dominated by film professionals with high expert reputations for making artistic films. Consequently the Gouden Kalf jury may be biased towards

giving awards to makers of artistic, as opposed to mainstream, films. Instead of the Academy Award jury that predominantly consists of other filmmakers with high market reputations and where Oscars influence the box-office success of mainstream films (Nelson et al., 2001) it might be that the Gouden Kalf awards influence the box-office success of art-house films (Gemser et al., 2008). The economic value of a Gouden Kalf in terms of additional box-office revenues might therefore be limited. Furthermore, the value of the award ceremony (Anand & Watson, 2004) of the Dutch Film Festival as such in legitimizing and promoting the overall Dutch film industry to a larger audience is therefore likely to be small. In future research it could be interesting to study how the composition of peer juries in terms of the dominance of its jury members' own market, expert or peer reputations determines the value of awards and awards ceremonies.

Chapter five shows that organizational *expectations* memory, or the web of expectations among members of an organization of being rewarded in the future for having invested in the organization in the present, is a precondition for the ability to build organizational *procedural* memory. Organizational procedural memory is an important mechanism for storing collective tacit knowledge or organization-specific knowledge. Because of its tacit and collective nature, organization-specific knowledge is a valuable resource that is difficult to imitate or transfer, and as such an important candidate for explaining performance differentials between organizations (Liebeskind, 1996) as postulated by the resource-based theory of the firm (Wernerfelt, 1984; Barney, 1991). Especially when individuals can identify with, and are loyal to, an organization they have more incentives to invest in organization-specific knowledge, the value of which they cannot themselves appropriate, since they expect the organization to reward them somewhere in the future (Simon, 1991). Yet this organizational expectations memory requires a certain degree of organizational continuity that seems to be lacking in project-based industries. The main finding of this chapter is that a latent organization, however, of individuals who serially collaborate in projects, and who are tied by implicit (MacNeil, 1980; Baker et al., 1997, 2002) and psychological contracts (Rousseau, 1989) allows for the formation of organizational expectations memory and, as a result, organizational procedural memory.

The former study has implications for the resource-based theory of the firm that ascribes competitive advantage, derived from valuable, inimitable, rare and non-substitutable resources, to formal organizations in the sense of legal entities (Barney, 1991). The resource-based theory of the firm has also been applied to network forms of organization in the continuum between stable hierarchically organized firms and market contracting, such as alliances between firms (Eisenhardt & Schoonhoven, 1996). The empirical findings of this study show that latent organizations in project-based industries are also capable of building unique, especially collective and tacit knowledge, resources. It might be that it is not so much the stability within or between formal *firms*, but the stability of relations between *individuals*, that allows for the build up of specific resources that are at the basis of a competitive advantage. Next, resources can be built and protected by either balancing internal and external labor mobility within the firm, by balancing stable alliance partners with new alliance partners, or a combination of both. The implications would then be that the core strategic issue is to optimally manage the social network of exchange partners, balancing strong ties necessary for building and protecting knowledge resources with weak ties needed to access new ideas that are crucial ingredients for remaining innovative and competitive.

### *Future research*

Besides the suggestions for further research already mentioned above there are some additional areas that might be promising.

First, in this thesis no evidence was found for status-based homophily selection in alliance formation between producers, directors and scriptwriters. In modeling the evolution of collaboration networks, however, only the effects of market and expert reputation were estimated. The effect of peer reputation, however, was not. The reason why the effect of peer reputation was not tested is that the Gouden Kalf award used for measuring peer reputation was introduced only recently for scriptwriters. Awards for directors and producers, on the other hand, have been around for a longer period of time. Although including peer reputation



would be interesting in itself, it would be even more so because it might allow for the disentanglement of status-based homophily selection based on similar peer reputations, and the effect of closeness or network position on tie formation. Both these effects might be two sides of the same coin. In other words, status-based homophily selection based on peer reputation may be highly correlated with the effect of network position on alliance formation. Sub-networks of individuals that are close to each other in the industry network might develop and share norms. Peer reputations of potential alliance partners, in turn, are the result of evaluations based on these norms. Closeness and similar peer reputation therefore might go hand in hand. A longitudinal network analysis approach applying SIENA should be able to disentangle these two related dynamics.

Second, it would be interesting to study organizational dynamics in social network in other industries. The television industry would be a logical extension of this study because it is closely linked to the film industry. Many professionals in the film industry are also active in the production of films and series for television (Storper, 1989). The networks of professionals in the film and television industry are therefore likely to overlap. Members of latent organizations in the film industry may possibly also be active in the television industry. Furthermore, if there turns out to be a status discrepancy between film and television this would allow latent organizations that are active in both industries to benefit from a finer grained quasi-internal labor market since it would increase the number of career steps or promotions. Career progression could be either a single step from the television to the film industry or a back and forth process between both industries. Second, it could be interesting to study what type of reputations in the television industry are most valuable in attracting investment capital and, possibly as a result, determine collaborative tie formations or alliances there. Finally, if the value of reputations is significantly different in the television industry as compared to the film industry while both industry networks partly overlap, this would further complicate competitive dynamics.

Third, it might be interesting to compare the findings of the Dutch film industry with that of other countries, especially the U.S. In the U.S. other types of reputations may be more valuable in obtaining capital for new films that in turn

shape the evolution of the industry network and the competitive environment. In the institutional environment of the U.S. film industry there is a stronger emphasis on making profits and therefore a tendency to invest in the production of commercially viable films. One would expect that market reputations are more valuable and therefore influential in shaping the evolution of the industry network and in determining success at different stages of the competitive process. If professionals with high market reputations are more successful in obtaining investment capital in the first stage, they will also be dominant in the second stage where films compete in the market for the end-user or consumer. This in turn would lead us to expect that peer juries at the Oscars are more inclined to reward films that are, or have the potential to, appeal to a large mainstream audience and become commercially successful. It would be interesting to find out what the value of different types of reputations is in the U.S. as compared to the Netherlands.

Fourth, it would be interesting to study how different types of reputations interact with one another, both in the film industry and other industries. First, is there a positive or negative interaction between different types of reputation, even if they are both positive? An example would be a film director with both a high expert and a high market reputation. It might be that, even though each of these reputations is valuable in isolation, having a clear or unambiguous identity based on one type of reputation is more valuable than a mixed one (Hsu & Hannan, 2005). On the other hand, as shown in chapter five, different types of reputation may have different value in different stages of the competitive process. Success would therefore be more likely to befall those who have different types of favorable reputations. Second, is the whole value of similar types of reputations larger than the sum of its parts? For example, an alliance between a film director and producer that both have favorable market reputations might increase the signal to consumers that their film is worth seeing, which in turn, would increase their bargaining position and ability to extract future rents. Third, can reputations of alliance partners be complementary? For example, a director with a favorable expert reputation might be more successful in obtain investment capital at the first stage of the competitive process, while a favorable market reputation of the producer

might lead to more success of the project in the second stage of vying for attention of the consumer.

Finally, it could be interesting to study the performance of latent organizations compared to normal organizations. This thesis has shown that latent organizations can bring certain benefits to its members and the organization as a whole, for example, in building organization-specific knowledge and organizational memory. This thesis did not, however, measure the performance of latent organizations at the level of the collective entity. Future research could compare the performance of latent organizations and 'normal organizations' such as Shell or General Motors. It will be challenging, however, to determine when performance can be ascribed to which latent organization since organizational membership and therefore the boundary of the latent organization are inherently dynamic and flexible. Yet normal organizations may encounter a similar challenge in terms of high levels of personnel turnover. Consequently, instead of the firm, it might make more sense to take social networks of employees and its structures as the level of analysis in explaining performance, especially if one believes that organizational performance derives from knowledge or human capital as suggested by proponents of the knowledge based view of the firm (Conner & Prahalad, 1996; Liebeskind, 1996).