

Determination

AlphaTheta and Serato [2024] NZCC 14

The Commission:	Dr John Small Anne Callinan Joseph Liava'a
Summary of application:	An application from AlphaTheta Corporation to acquire 100% of the shares in Serato Audio Research Limited.
Determination:	Under section 66(3)(b) of the Commerce Act 1986, the Commerce Commission declines to give clearance for the acquisition.
Date of determination:	17 July 2024

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Executive summary

- X1. The Commerce Commission (Commission) declines to give clearance for AlphaTheta Corporation (ATC) to acquire 100% of the shares in Serato Audio Research Limited (Serato) (the Proposed Acquisition). The Commission is not satisfied that the Proposed Acquisition would not have, or would not be likely to have, the effect of substantially lessening competition in the DJ software and DJ hardware markets in New Zealand.
- X2. The Proposed Acquisition would bring together two DJ software providers that supply DJ software for use on laptops. The Parties compete closely for the supply of these products, and post-acquisition the merged entity would have a high market share in the supply of DJ software in New Zealand. The Proposed Acquisition would eliminate the current competitive constraint between the Parties, and we are not satisfied that, compared with the counterfactual where the Proposed Acquisition did not proceed, the remaining competitive constraints in the relevant markets would be likely to impose sufficient constraint on the merged entity so that a substantial lessening of competition is unlikely.
- X3. The DJ software competitors that would compete with the merged entity post-acquisition – including VirtualDJ, Traktor and Algoriddim – would be significantly smaller than the merged entity or have products that are viewed as being for beginner DJs, or both. These DJ software providers would be unlikely to constrain the merged entity in their current guise, or be capable of expanding, to sufficiently replace the competition lost with the Proposed Acquisition. We also consider it unlikely that new entry would occur to sufficiently replace this lost competition. Further, there is limited evidence to suggest that mobile apps impose a constraint on the Parties, or will do so in the future.
- X4. As explained in more detail later in this determination, the loss of competition caused by the Proposed Acquisition would be likely to result in unilateral effects, enabling the merged entity to raise prices for DJ software significantly and/or reduce the quality of its DJ software offerings significantly, such as by reducing the level of innovation and introduction of new product features that would occur in the counterfactual.
- X5. The Proposed Acquisition would also represent a merger of the most popular DJ software brand (Serato) with the most popular DJ hardware brand (ATC's Pioneer DJ), and we are not satisfied that it would not substantially lessen competition by way of vertical effects.
- X6. Serato is an important piece of DJ software for DJ hardware providers to integrate their products with, and we are not satisfied that, post-acquisition, the merged entity would not have the ability and incentive to foreclose rival suppliers of DJ hardware by refusing to supply them with Serato, or supplying them on materially worse terms than it supplies itself. This would make rival DJ hardware suppliers' products significantly less attractive to consumers, and therefore substantially lessen competition.

- X7. Finally, our investigation found that the merged entity would gain access to its DJ hardware competitors' commercially sensitive information through the integration process of those DJ hardware providers' products with Serato software. We are not satisfied that this would be unlikely to substantially lessen competition by substantially reducing the incentive for the merged entity's competitors to innovate, for fear of disclosing commercially sensitive information to the merged entity. It could also reduce the merged entity's incentive to innovate.

The Proposed Acquisition

Summary of the Proposed Acquisition

1. On 10 October 2023, the Commerce Commission (Commission) registered a clearance application (the Application) from AlphaTheta Corporation (ATC) seeking clearance to acquire 100% of the shares in Serato Audio Research Limited (Serato) (the Proposed Acquisition).¹ We refer to ATC and Serato together as ‘the Parties’.

Applicant’s rationale for the merger

2. ATC submitted that, from its perspective, a key driver of the acquisition is to enable ATC to benefit from Serato’s experience in music production, helping ATC to expand in that segment of the music industry.²

Our decision

3. The Commission declines to give clearance to the Proposed Acquisition as it is not satisfied that the Proposed Acquisition will not have, or would not be likely to have, the effect of substantially lessening competition in a market in New Zealand.

Our framework

4. Our approach to analysing the competition effects of mergers is based on the principles set out in our Mergers and Acquisitions Guidelines.³

The substantial lessening of competition test

5. As required by the Commerce Act 1986 (Act), we assess mergers using the substantial lessening of competition test.
6. We determine whether a merger is likely to substantially lessen competition in a market by comparing the likely state of competition if the merger proceeds (the scenario with the merger, often referred to as the factual), with the likely state of competition if the merger does not proceed (the scenario without the merger, often referred to as the counterfactual).⁴
7. We make a pragmatic and commercial assessment of what is likely to occur in the future, with and without the merger, based on the information we obtain through our investigation and taking into account factors such as market growth and technological changes.⁵
8. A lessening of competition is generally the same as an increase in market power. Market power is the ability to raise price above the price that would exist in a

¹ A public version of the Application is available on our website at: <http://www.comcom.govt.nz/business-competition/mergers-and-acquisitions/clearances/clearances-register/>.

² The Application at [3.8].

³ Commerce Commission, Mergers and Acquisitions Guidelines (May 2022).

⁴ *Commerce Commission v Woolworths Limited* (2008) 12 TCLR 194 (CA) at [63].

⁵ Mergers and Acquisitions Guidelines above n3 at [2.35].

competitive market (the ‘competitive price’),⁶ or reduce non-price factors such as quality or service below competitive levels.

9. Determining the scope of the relevant market or markets can be an important tool in determining whether a substantial lessening of competition is likely.
10. We define markets in the way that we consider best isolates the key competition issues that arise from the merger. In many cases this may not require us to precisely define the boundaries of a market. A relevant market is ultimately determined, in the words of the Act, as a matter of fact and commercial common sense.⁷

When a lessening of competition is substantial

11. Only a lessening of competition that is substantial is prohibited. A lessening of competition will be substantial if it is real, of substance, or more than nominal.⁸ Some courts have used the word ‘material’ to describe a lessening of competition that is substantial.⁹
12. Consequently, there is no bright line that separates a lessening of competition that is substantial from one which is not. What is substantial is a matter of judgement and depends on the facts of each case.¹⁰ We often assess the likelihood of competition being substantially lessened by asking whether consumers in the relevant market(s) are likely to be affected in a material way.

When a substantial lessening of competition is likely

13. A substantial lessening of competition is ‘likely’ if there is a real and substantial risk, or a real chance, that it will occur. This requires that a substantial lessening of competition is more than a possibility but does not mean that the effect needs to be more likely than not to occur.¹¹

The clearance test

14. We must clear a merger if we are satisfied that the merger would not be likely to substantially lessen competition in any market.¹² If we are not satisfied – including if we are left in doubt – we must decline to clear the merger.
15. In *Woolworths* the Court of Appeal held that “the existence of a ‘doubt’ corresponds to a failure to exclude a real chance of a substantial lessening of competition”.¹³
16. The burden of proof lies with ATC, as the applicant, to satisfy us on the balance of probabilities that the merger is not likely to have the effect of substantially lessening

⁶ Or below competitive levels in a merger between buyers.

⁷ Section 3(1A). See also *Brambles v Commerce Commission* (2003) 10 TCLR 868 at [81].

⁸ *Woolworths & Ors v Commerce Commission* (2008) 8 NZBLC 102,128 (HC) at [127].

⁹ *Woolworths & Ors v Commerce Commission* (HC) above n8 at [129].

¹⁰ Mergers and Acquisitions Guidelines above n3 at [2.23].

¹¹ *Woolworths & Ors v Commerce Commission* (HC) above n8 at [111].

¹² Commerce Act 1986, s 66(3)(a).

¹³ *Commerce Commission v Woolworths Ltd* (CA) above n4 at [98].

competition.¹⁴ The decision to grant or refuse a clearance is necessarily to be made on the basis of all of the evidence.¹⁵ We will sometimes have before us conflicting evidence from different market participants and must determine what weight to give the evidence of each party.¹⁶

17. A lessening of competition does not need to be felt across an entire market, or relate to all dimensions of competition in a market, for that lessening to be substantial. A lessening of competition that adversely affects a significant section of the market may be enough to amount to a substantial lessening of competition.¹⁷
18. We often assess competition effects over the short term (ie, two years). The relevant timeframe for assessment will, however, depend on the circumstances. A longer timeframe will be appropriate if, on the evidence, competition effects are likely to arise in later years.¹⁸
19. A lessening of competition or an increase in market power may manifest itself in a number of ways, including higher prices or reduced services.¹⁹

The Parties

ATC

20. ATC is a global company headquartered in Japan. It develops, manufactures and sells DJ hardware as well as DJ software.
21. ATC sells its DJ hardware products (such as DJ players, mixers, controllers, all-in-one systems, turntables and audio interfaces). Until recently, ATC's hardware was sold under the Pioneer DJ brand. However, ATC has now started selling products under the "AlphaTheta" brand.²⁰
22. ATC's laptop application DJ software is called rekordbox. DJs can use rekordbox to organise their music library, create playlists and prepare tracks, and can also use rekordbox when mixing music and performing live. rekordbox's laptop application software is available as a free plan (rekordbox Free) and on three different tiers of paid plans (Core, Creative and Professional).²¹ rekordbox Free can only be used with

¹⁴ *Commerce Commission v Southern Cross Medical Care Society* (2001) 10 TCLR 269 (CA) at [7] and *Commerce Commission v Woolworths Ltd* (CA) above n4 at [97].

¹⁵ *Commerce Commission v Woolworths Ltd* (CA) above n4 at [101].

¹⁶ *Brambles New Zealand Ltd v Commerce Commission* above n7 at [64].

¹⁷ *Dandy Power Equipment Pty Ltd v Mercury Marine Pty Ltd* (1982) 64 FLR 238; ATPR 40-315, 43, 888.

¹⁸ *Woolworths & Ors v Commerce Commission* (HC) above n8 at [131]. See also Merger and Acquisitions Guidelines at [3.106], in the context of the LET test: "The appropriate timeframe may vary from market to market according to the particular characteristics of the market concerned. For example, in some markets where products are supplied and purchased on a long-term contractual basis, customers may not immediately be exposed to the detrimental effects stemming from a potential substantial lessening of competition. In such cases, the competition analysis, in a timing sense, begins with the point at which those contracts come up for renewal" (footnotes omitted).

¹⁹ Merger and Acquisitions Guidelines above n3 at [2.21].

²⁰ ATC "AlphaTheta brand introduction" (press release, 23 January 2024).

²¹ The Application at [4.7].

Pioneer DJ hardware but the other rekordbox plans can be used with some non-Pioneer DJ hardware.

23. ATC has also developed a mobile app version of its rekordbox software as well as another mobile app called WeDJ.
24. Pioneer DJ hardware and rekordbox software are available worldwide.

Serato

25. Serato is a DJ and music production software company that was founded in New Zealand in 1999. Serato's DJ software is available worldwide and is integrated with over 90 pieces of DJ hardware made by various companies, including ATC's Pioneer DJ.
26. As described in the Application, Serato's software products include:²²
 - 26.1. Serato DJ Lite – a free version of Serato software “for learning” that can be used with or without hardware.
 - 26.2. Serato DJ Pro – Serato's “flagship” professional DJ software used by hobbyist DJs through to professional DJs. The main features of Serato DJ Pro are music management, music analysis and playing and mixing music. Serato DJ Pro can be purchased outright or as a monthly subscription.
 - 26.3. Serato DJ Suite – an all-in-one suite of expansion packs for Serato DJ Pro that provide enhanced functionality, including Serato Video (allows DJs to incorporate visual effects) and Serato FX (access to custom sound effects). Serato DJ Suite can be purchased outright or as a monthly subscription.
27. Serato also has music production software called Serato Studio.

Industry background

DJ software

28. DJ software can be used to create various effects when mixing different songs and for organising music ahead of mixing (for example, creating playlists and preparing tracks to be exported).
29. DJ software is typically integrated into a piece of DJ hardware or installed onto a laptop, mobile phone or tablet, and can be used with or without connecting the device to a piece of DJ hardware.

²² The Application at [4.27].

30. The types of software used for DJing can be:
- 30.1. software for use on a laptop or desktop computer that can either be used standalone or with DJ hardware (we refer to this type of software as a 'laptop application');
 - 30.2. software for use on a mobile phone or tablet that can either be used standalone or with some forms of DJ hardware (we refer to this type of software as a 'mobile app'); or
 - 30.3. software that is embedded on a piece of DJ hardware for use on that piece of hardware only (we refer to this type of software as 'embedded software').

DJ hardware

31. DJ hardware helps DJs to mix and remix music. DJs typically use some form of DJ hardware to control what happens with the DJ software.²³ DJs will also require access to music, which can be stored on a USB stick or a laptop, tablet or mobile phone.
32. Hardware used for DJing includes the following equipment:
- 32.1. DJ player (or CDJs)²⁴ – enables DJs to play digital music. As DJ players have embedded software they do not require an external piece of software and can simply be used with a USB stick with music on it.
 - 32.2. Mixer – used to control and manipulate music from multiple sources. Mixers are used with DJ players and turntables to mix music.
 - 32.3. Controller – portable devices normally containing two jog wheels (which emulate turntables) and controls to enable mixing music. Controllers must be connected to a device (such as a laptop, mobile or tablet) to access music.
 - 32.4. All-in-one system – combines DJ players and mixers into a single device. All-in-one systems may access music via a USB stick or may be connected to a device such as a laptop.
 - 32.5. Turntable – used to play vinyl records.
 - 32.6. Audio interface – used to convert a source of audio from one type to another, for example converting an analogue signal from a vinyl record into a digital signal that can be received by a laptop.

Customers

33. Customers range from DJs who are just starting out (beginners), those who are either DJing for fun or with the aim of turning professional or semi-professional

²³ As we note at paragraph [34], DJs can also DJ using only DJ hardware or only DJ software.

²⁴ DJ players are also known as 'CDJs' reflecting that historically they were used to play music stored on CDs. DJs now often use USBs to store music and some devices do not have CD slots.

(hobbyists), through to those that make a full or partial living from DJing (such as DJs that tour the world or wedding/event DJs) (professionals).

34. DJs will commonly use some form of DJ hardware in conjunction with DJ software, however DJs may also DJ using only hardware (such as CDJs in conjunction with a USB stick with music on it) or only software (such as using a laptop with software installed). DJs tend to use different types of equipment based on their level of expertise. As DJs grow in experience, they may wish to upgrade their setups to more 'professional' software/hardware.

Other DJ software providers

35. Participants in the DJ software industry aside from Serato and rekordbox include:

- 35.1. VirtualDJ – a French DJ software company. VirtualDJ's laptop application software is not integrated with any DJ hardware prior to the hardware's release but is compatible with DJ hardware from all the main DJ hardware brands (ie, it is integrated with these products after their release).
- 35.2. Native Instruments (also present in DJ hardware) – a German company that produces Traktor laptop application software. Traktor is integrated with Native Instruments hardware (controllers and mixers) and is compatible with third-party controllers from brands such as Pioneer DJ, Denon DJ, Numark, Reloop and Rane.
- 35.3. Algoriddim – a German company that produces djay, which is software that is available as a laptop application and a mobile app. djay is integrated with certain pieces of hardware from Pioneer DJ, Reloop and Hercules.²⁵
- 35.4. inMusic (also present in DJ hardware) – a US company that produces Engine DJ, which is software that is available as a laptop application and embedded software. Engine DJ only integrates with inMusic's own hardware (Denon DJ and Numark).
- 35.5. Hercules (also present in DJ hardware) – a French company that produces DJUCED laptop application DJ software. DJUCED only integrates with Hercules' own hardware.

Other DJ hardware providers

36. Participants in the DJ hardware industry aside from ATC include:

- 36.1. Native Instruments (also present in DJ software) – a German company that produces DJ hardware including controllers, mixers and audio interfaces.

²⁵ Such as Pioneer DJ's DDJ-FLX4 and DDJ-200, Reloop's Mixtour Pro and Mixon 8 Pro and Hercules' DJControl Mix.

- 36.2. inMusic (also present in DJ software) – a US company that produces DJ players, mixers, controllers, all in one DJ systems, turntables and audio interfaces under the Rane, Denon DJ, Numark and Akai brands.
- 36.3. Reloop – a German company that produces controllers, mixers, turntables, speakers and audio interfaces.
- 36.4. Roland – a Japanese manufacturer of controllers and other types of music performance hardware.
- 36.5. Hercules (also present in DJ software) – a French manufacturer of controllers and other types of music performance hardware.

Interoperability among DJ software and DJ hardware products

- 37. There are several industry participants that are active in both the DJ hardware and software spaces. Where this is the case, in some instances the company's DJ software will only be able to be used with that company's DJ hardware (for example, inMusic's Engine DJ software can only be used with inMusic hardware) but in other instances, a brand's DJ software can be used with other providers' hardware (for example, Native Instrument's Traktor software can be used with other DJ hardware). All DJ hardware can be used with a range of DJ software, even when the DJ hardware provider also has their own DJ software product.
- 38. DJ software and DJ hardware brands will commonly partner to integrate their products. Integration of DJ software with DJ hardware makes for a more seamless experience for the user and can be a selling point for the hardware. The DJ hardware and software combination works straight away without the DJ being required to take any steps to ensure compatibility. This is known as "plug and play". The DJ hardware provider will list the DJ software products that are officially supported by the device and in some cases the device will carry the brand of the DJ software.²⁶ The integration process can happen before or after the DJ hardware launches. Where it occurs beforehand, the firms may spend many months working together to create the overall product and/or special features that another hardware brand might not offer. Integration may also occur after launch to make other software compatible with the hardware.
- 39. DJ software companies can also make their products compatible with DJ hardware without official support. Some DJ hardware uses the MIDI (Musical Instrument Digital Interface) communication standard and DJ software companies can design products that can function with those devices. However, without directly working with the DJ hardware provider, the DJ hardware devices may not work perfectly with the software. In addition, the DJ hardware and software will not work straight away – DJs will have to carry out additional steps (often called 'MIDI mapping' or 'configuring') to make the DJ hardware and software work together.

²⁶ For example, ATC's Pioneer DJ DDJ-REV5 controller carries the Serato logo and Reloop's Buddy controller carries the Algoriddim logo.

Market definition

40. We consider that the markets relevant to the assessment of the competitive effects of the Proposed Acquisition are the:
 - 40.1. national market for the supply of DJ software (including laptop applications but excluding mobile apps and music production software) (the DJ software market); and
 - 40.2. national market for the supply of controllers and all-in-one systems (the DJ hardware market).

41. The main market definition issue we have assessed is whether it is appropriate to include mobile apps in the same market as laptop applications. As we discuss in further detail below, we conclude that mobile apps are not in the DJ software market because:
 - 41.1. mobile apps have less functionality than laptop applications;
 - 41.2. mobile apps are less likely to integrate with controllers;
 - 41.3. mobile apps appear to be targeted at a different customer group to laptop applications (beginners); and
 - 41.4. there is limited evidence that the rise of mobile apps has imposed a competitive constraint on suppliers of laptop applications, in particular, there is:
 - 41.4.1. limited evidence of consumers of laptop applications switching to mobile apps; and
 - 41.4.2. limited evidence that mobile apps will grow in popularity in the period relevant to our assessment²⁷ such that they are likely to be a significant constraint on laptop applications.

Our approach to market definition

42. Market definition is a tool that helps to identify and assess the competitive constraints that the merged entity would face post-acquisition. Determining the relevant market requires us to judge whether, for example, two products are sufficiently close substitutes in demand and/or supply as a matter of fact and commercial common sense so as to fall within the same market.

43. We use the so-called hypothetical monopolist test as a conceptual tool to help identify a relevant market. We ask if a hypothetical monopolist of the product in question could profitably impose a small but significant non-transitory increase in price (a 'SSNIP').²⁸ A hypothetical monopolist will be unable to profitably impose a

²⁷ Including once the earn out provisions of the agreement between the Parties expires in 2028.

²⁸ Or an equivalent reduction in quality.

SSNIP on the product in question if there is sufficient demand-side substitution to alternative products and/or sufficient supply-side substitution from alternative products.

- 43.1. Demand-side substitution is the extent to which buyers of the product in question would switch to alternative products in response to a SSNIP.
- 43.2. Supply-side substitution is the extent to which rival firms would easily, profitably and quickly (generally within one year) switch production to the product in question in response to a SSNIP.²⁹
44. If the hypothetical monopolist could not profitably impose a SSNIP on the product because of demand or supply side substitution, the boundaries of the market are expanded to include the next closest substitute. The process is repeated, and the group of products included in the market expanded, until the hypothetical monopolist supplier could profitably impose a SSNIP.
45. The purpose of defining a market is to help identify the constraints on the merged entity in areas where competitive harm may occur. For unilateral effects, the 'product in question' at which we start the hypothetical monopolist test is normally the product(s) where there is competitive overlap between the parties. The overlap between the Parties in this case is the supply of laptop DJ software applications. That is the starting point for assessing the relevant market in respect of DJ software. We may also need to define markets for any complementary products that the firms supply where vertical and/or conglomerate effects may arise (here, various types of DJ hardware). In this case, the 'product in question' at which we start the hypothetical monopolist test will be the DJ hardware supplied by ATC.
46. We define markets in the way that we consider best isolates the key competition issues that arise from a merger.³⁰ In some cases it may not be possible to precisely identify the market's boundaries and which products are within the market and which are outside. However, the overall assessment of the Proposed Acquisition will not be affected by the chosen market definition because we take into account constraints from all sources, whether they are ultimately found to be located inside or outside the relevant market. What matters is that we consider all relevant competitive constraints, and the extent of those constraints.

²⁹ Mergers and Acquisitions Guidelines above n3 at [3.16].

³⁰ Mergers and Acquisitions Guidelines above n3 at [3.10].

The DJ software market

ATC's views

47. ATC submitted that the relevant product market is the supply of DJ software to end users, which includes:³¹
- 47.1. all types of specialist DJ software solutions including laptop applications and mobile apps written for iOS (Apple) and Android systems, that are designed to be used on a mobile or tablet; and
 - 47.2. both DJ and music production software.
48. ATC submitted that the relevant market for DJ software includes mobile apps. ATC made several arguments in support of this.
49. First, ATC submitted that mobile apps offer similar functionality to laptop applications.
- 49.1. It submitted that there are two main functions of DJ software, which are preparation (organising, preparing libraries and editing/remixing songs) and performance (ie, live DJing). ATC said DJs can use mobile apps for both of these functions.
 - 49.1.1. While DJs may still prefer to prepare music on laptops, mobile apps are becoming increasingly popular for preparation.
 - 49.1.2. Mobile apps provide all the functionality and processing power required for the performance function, and have some advantages (such as the ability to immediately start mixing from personal libraries and the engagement available from a touchscreen).³²
 - 49.2. ATC further submitted that, while mobile devices have a smaller screen size than laptops, this is irrelevant for performance because DJs limit their interaction with the laptop when performing.³³ ATC submitted that the touch screen of mobiles may be preferred by new DJs who have grown up with that technology.³⁴
 - 49.3. Finally, it submitted that mobile apps (in particular Algoriddim) are compatible with many controllers (and conversely many laptop applications are not) and DJ hardware providers promote compatibility with mobile apps for some products.³⁵

³¹ The Application at [5.22].

³² ATC "Submission by AlphaTheta Corporation on the Statement of Issues" (8 April 2024) at [4.27]-[4.28].

³³ ATC "Submission by AlphaTheta Corporation on the Statement of Issues" (8 April 2024) at [4.24]-[4.28].

³⁴ ATC "Submission by AlphaTheta Corporation on the Statement of Issues" (8 April 2024) at [4.28].

³⁵ ATC "Submission by AlphaTheta Corporation on the Statement of Issues" (8 April 2024) at [4.29]-[4.37].

50. Second, ATC submitted that mobile apps offer an alternative for all types of DJs, not just beginners.

50.1. According to ATC, there are many mobile apps that are targeted towards experienced DJs and there are examples of well-known DJs using mobile apps for performing.³⁶

50.2. ATC submitted that []:³⁷

50.2.1. [

50.2.2.

50.2.3.

].

51. ATC submitted that there is significant supply side substitution between laptop applications and mobile apps, with numerous examples of developers of laptop applications expanding into mobile apps.³⁸

52. Third, ATC submitted that the evidence shows that mobile apps impose a competitive constraint on laptop applications.

52.1. ATC submitted that mobile apps compete with laptop applications through innovation. ATC said the evidence shows that []:³⁹

52.1.1. ATC submitted that the competitive threat posed by mobile apps on laptop applications led to it launching a new version of its rekordbox

³⁶ ATC "Submission by AlphaTheta Corporation on the Statement of Issues" (8 April 2024) at [4.17].

³⁷ Email from ATC with comments on unredacted SoUI (20 June 2024).

³⁸ For example, ATC said that Algoriddim's djay was originally launched as MacBook OS DJ software and later expanded into an iOS app, Native Instruments launched its Traktor DJ app in 2013 and ATC released WeDJ and its rekordbox mobile app after developing its rekordbox laptop application (ATC "Submission by AlphaTheta Corporation on the Statement of Issues" (8 April 2024) at [4.49]).

³⁹ ATC "Confidential submission on Confidential Sol" (9 April 2024) at [1] of Appendix 1.

mobile app in 2023 that included performance functionality.⁴⁰ ATC told us that:⁴¹

52.1.1.1. [

52.1.1.2.

52.1.1.3.

].

52.2. ATC submitted that the growth of laptop applications would have been higher without mobile apps.⁴²

53. ATC submitted that embedded software (software that comes with “all-in-one” systems) and music production software should also be included in the market, as excluding them does not reflect the facts or make commercial common sense.⁴³

53.1. Embedded software (such as inMusic’s Engine DJ) that comes with all-in-one systems allows DJs to carry out core DJ performance functionality.⁴⁴

53.2. Music production software (such as Ableton) can be used for editing music and for preparation and is also used by some DJs for performance.⁴⁵

54. ATC submitted that the supply of DJ hardware and DJ software take place on a global basis, however for the purposes of its assessment of the Proposed Acquisition in the Application it has focused on a national market (New Zealand).⁴⁶

⁴⁰ ATC “Submission by AlphaTheta Corporation on the Statement of Issues” (8 April 2024) at [4.11].

⁴¹ ATC RFI response (6 June 2024) at pp. 5-6.

⁴² ATC “Submission by AlphaTheta Corporation on the Statement of Issues” (8 April 2024) at [4.44]-[4.47].

⁴³ ATC “Submission by AlphaTheta Corporation on the Statement of Issues” (8 April 2024) at [1.5(a)].

⁴⁴ ATC “Submission by AlphaTheta Corporation on the Statement of Issues” (8 April 2024) at [4.52].

⁴⁵ ATC “Submission by AlphaTheta Corporation on the Statement of Issues” (8 April 2024) at [5.5].

⁴⁶ The Application at [5.29]-[5.30].

Serato's views

55. Serato also submitted that the market for DJ software includes mobile apps.
56. First, Serato submitted that mobile apps have the same functionality as laptop applications. Serato submitted that:⁴⁷
- 56.1. mobile apps are functionally identical to Serato's laptop application;
 - 56.2. DJs can perform using a laptop or mobile phone interchangeably; and
 - 56.3. mobile apps are compatible with a wide range of DJ hardware.
57. Second, Serato submitted that mobile apps being attractive to the "next generation" of DJs should not be interpreted as mobile apps only being suitable for beginners.⁴⁸
58. Serato considers that there are multiple ways to DJ (such as using vinyl, CDJs, laptops and mobiles/tablets) and that from an audience perspective, there is no need to distinguish between any of these methods. Serato considers that 'laptop DJing' is an artificial construct that does not exist outside of the assessment of the Application because audiences are indifferent to whether DJs use a laptop or mobile device.⁴⁹
59. Serato submitted that different DJs have different preferences about how to DJ, and a DJ choosing to continue DJing with a laptop rather than changing to a mobile app does not mean that mobile apps are in a separate market.⁵⁰ Serato submitted that the variety of options consumers have drives Serato to ensure that its product is the best it can be.⁵¹ Serato submitted that mobile apps are facing a similar resistance from existing DJs that laptop DJing initially faced when it first appeared as an option, and that, as laptop DJing is now mainstream, mobile apps will in time also become mainstream.⁵²
60. Serato submitted that it not having a mobile app does not suggest that mobile apps belong in a separate market:
- 60.1. Serato would like to develop a mobile app [

].⁵³
 - 60.2. [

].⁵⁴

⁴⁷ Serato "Submission on Statement of Unresolved Issues" (17 June 2024) at [18].

⁴⁸ Serato "Submission in response to Commerce Commission Statement of Issues" (8 April 2024) at [56].

⁴⁹ Serato "Submission on Statement of Unresolved Issues" (17 June 2024) at [13].

⁵⁰ Serato "Submission on Statement of Unresolved Issues" (17 June 2024) at [14].

⁵¹ Serato "Submission on Statement of Unresolved Issues" (17 June 2024) at [15].

⁵² Serato "Submission on Statement of Unresolved Issues" (17 June 2024) at [16]-[17].

⁵³ Serato "Submission on Statement of Unresolved Issues" (17 June 2024) at [21].

⁵⁴ Serato "Submission in response to Commerce Commission Statement of Issues" (8 April 2024) at [48].

- 60.3. Not having a mobile app puts Serato at a competitive disadvantage, but it remains competitive by ensuring its laptop application is the best it can be.⁵⁵

Our assessment of the DJ software market

61. As noted earlier, market definition is a tool that helps us to identify the constraints on the merged entity. The competitive overlap between the Parties is for laptop applications and, accordingly, that is the starting point for our assessment. To assess whether we should expand the boundaries of the relevant product market beyond this point, we have asked whether sufficient customers of laptop applications would viably switch to alternatives (such as mobile apps) in response to a SSNIP in the price of laptop applications so that the SSNIP would not be profitable.
62. We have considered whether mobile apps should be included in the relevant market. Based on the evidence before us, we are not satisfied that mobile apps are, or will be in the period relevant to this assessment, a sufficiently close substitute for laptop applications such that they belong in the relevant DJ software market. As we describe in more detail below, this is for the following reasons:
- 62.1. mobile apps have less functionality than laptop applications;
- 62.2. mobile apps are less likely to integrate with controllers;
- 62.3. mobile apps appear to be targeted at a different customer group (beginners);
- 62.4. there is limited evidence that the rise of mobile apps has imposed a competitive constraint on suppliers of laptop applications, in particular, there is:
- 62.4.1. limited evidence of consumers of laptop applications switching to mobile apps; and
- 62.4.2. limited evidence that mobile apps will grow in popularity in the period relevant to our assessment⁵⁶ such that they are likely to be a significant constraint on laptop applications.

Mobile apps have less functionality than laptop applications

63. The Parties submitted that mobile apps offer the same functionality as laptop applications. We do not agree. The evidence we have gathered indicates that mobile apps offer less functionality compared to laptop applications. The extent of differences depends on the particular mobile app (with Algoriddim being the most feature rich mobile app). We consider the evidence indicates that many users of laptop applications perceive mobile apps as being inferior and would be unwilling to switch to them in response to a SSNIP in the price of laptop applications.

⁵⁵ Serato "Submission on Statement of Unresolved Issues" (17 June 2024) at [21].

⁵⁶ Including once the earnout provisions of the agreement between the Parties expires in 2028.

64. The main differences in functionality that were identified during the investigation are the following:
- 64.1. Although mobile apps have many of the same features as laptop applications like Serato, rekordbox and VirtualDJ, they do not have all of them.⁵⁷ For example, it appears that the only mobile app to offer the feature stems (which allows the DJ to separate out and individually play the different components of a song, for example vocals, drums or bassline) is Algoriddim's djay. rekordbox's mobile app does not have stems, despite its laptop application having this feature.⁵⁸
 - 64.2. Mobile devices have smaller screens which reduces what they can display.⁵⁹ However, as the Parties note, mobile apps can also be used on tablets, which have a screen that of a similar size to laptops. At any rate, the Parties submitted the screen size does not matter for performance where DJs avoid interacting with the device.⁶⁰ We recognise that the smaller size of the device may be an advantage in some scenarios, for example, where the DJ values portability. However, we consider screen size may be more relevant when the device is being used for preparation. As ATC acknowledges, DJs may still prefer using a laptop for preparation than mobile apps.⁶¹
 - 64.3. Although the Parties submitted that most mobile devices have sufficient processing power,⁶² we consider that mobile devices have less processing power than laptops which may increase the risk of latency and limit the features that the DJ can use.⁶³ Mobile devices may also be limited by storage capacity, and some DJs may find it comparatively slower to search for songs on a mobile than on a laptop.⁶⁴

Mobile apps are less likely to be integrated with DJ hardware

65. The ability for a DJ using laptop applications to switch to mobile apps will also be limited by whether the mobile app is compatible with the DJ hardware the DJ is using. Most controllers do not come already integrated, and ready to work, with

⁵⁷ See for example NERA Economic Consulting "AlphaTheta Corporation/Serato: unilateral effects and foreclosure theories of harm" (27 November 2023) at Table 2.4 and ATC "Submission by AlphaTheta Corporation on the Statement of Issues" (8 April 2024) Table 1.

⁵⁸ ATC "Submission by AlphaTheta Corporation on the Statement of Issues" (8 April 2024) Table 1.

⁵⁹ Commerce Commission interview with [redacted]. One DJ thought this would make it harder to DJ, as it can be harder to find and locate songs to play (Commerce Commission interview with [redacted]).

⁶⁰ ATC "Submission by AlphaTheta Corporation on the Statement of Issues" (8 April 2024) at [4.24]-[4.28] and Serato "Submission in response to Commerce Commission Statement of Issues" (8 April 2024) at [29].

⁶¹ ATC "Submission by AlphaTheta Corporation on the Statement of Issues" (8 April 2024) at [4.27]-[4.28].

⁶² ATC "Submission by AlphaTheta Corporation on the Statement of Issues" (8 April 2024) at [4.27].

⁶³ For example [redacted] advised that did not develop for Android because it could not handle latency (Commerce Commission interview with [redacted]). A DJ we spoke thought mobile devices might lack the processing power of a laptop that could be necessary to run features such as real time stems. Commerce Commission interview with [redacted].

⁶⁴ Commerce Commission interviews with [redacted] and [redacted]. [redacted] noted that younger DJs would likely be more adept at searching on a mobile phone than a laptop.

mobile apps. For example, only three Pioneer DJ hardware devices are integrated with mobile apps (even including ATC’s rekordbox mobile app) all of which are low-priced controllers.⁶⁵ For the remaining Pioneer DJ devices, consumers will have to carry out work on their end to make the hardware device and mobile app compatible.⁶⁶ If mobile apps are a close substitute for laptop applications for users of controllers we would expect that a greater number of controllers would have official integration with mobile apps.

66. We asked ATC for further information on the mobile apps that are compatible with Pioneer DJ hardware, and which mobile app producers ATC had approached, and been approached by, for integration. In response, ATC said that:⁶⁷

66.1. []
[]
].

66.2. []
[]
].⁶⁸

66.3. []
[]
[]
].⁶⁹

⁶⁵ The controllers with official mobile app integration are the DDJ-200, DDJ-400 and DDJ-FLX4.
⁶⁶ [] and [] told us that it is not possible to MIDI map (manually assign buttons on a hardware product to control features of the software) DJ hardware to mobile apps that are not officially supported (Commerce Commission interviews with [] and []). If so, this would further limit the opportunity for DJs using hardware to switch to using mobile apps. However, even if DJs are able to do this, MIDI mapping is unlikely to be a substitute for full integration as it does not allow for the same depth integration and may result in a lower quality outcome for the user. We discuss MIDI mapping further at paragraph [225].

⁶⁷ ATC RFI response (6 June 2024) at pp. 8-9.

⁶⁸ []

⁶⁹ []
ATC RFI response (17 June 2024). []

67. The Parties submitted that Algoriddim is compatible with many controllers.⁷⁰ Of the mobile apps, Algoriddim seems to be the most feature rich and has versions that can be used on many platforms including Windows laptops, Apple laptops and mobile phones/tablets running iOS and Android. Algoriddim is also the mobile app with the most official integrations with Pioneer DJ hardware.

68. However, [

].⁷¹ [

].⁷² [

].⁷³

Mobile apps are targeted at a different customer group

69. The evidence indicates that mobile apps are targeted at a different type of customer than laptop applications.⁷⁴ The market feedback suggests that mobile apps are focused on beginners whereas laptop applications are focused on more advanced users.⁷⁵ As we explain below, while in principle mobile apps could nevertheless impose a constraint despite being focused on beginners, we did not see evidence of that constraint.

70. Internal documents from ATC indicate it [].

70.1. An ATC internal document suggests that [], stating:⁷⁶

70.1.1. [

].

⁷⁰ ATC “Submission by AlphaTheta Corporation on the Statement of Issues” (8 April 2024) at [6.12(c)] and Serato “Submission in response to Commerce Commission Statement of Issues” (8 April 2024) at [31]-35].

⁷¹ [].

⁷² [].

⁷³ [].

⁷⁴ Commerce Commission interviews with [], [] and [].

⁷⁵ Another way to assess the constraint from mobile apps would be to consider whether there were separate customer markets for beginners and more advanced users. However, we consider our approach (that considers whether there are separate product markets for laptop applications and mobile apps) is also an appropriate way to take into account the constraint of mobile apps on the merged entity.

⁷⁶ [].

70.1.2.

70.1.3.

].

70.2. In emails between ATC and [] and ATC and [] that were exchanged during the integration process, ATC mentions:

70.2.1. [

].⁷⁷

70.2.2. [

].⁷⁸

70.2.3. [

].⁷⁹

70.3. An ATC planning document for [] notes that:

70.3.1. [

];⁸⁰

70.3.2. [

];⁸¹

70.3.3. [

];⁸² and

77 [].
78 [].
79 [].
80 [].
81 [].
82 [].

70.3.4. [

].⁸³

71. Market participants generally viewed mobile apps as being targeted at beginners.

71.1. [] told us that mobile apps are a “different world” to laptop applications. It said mobile apps are for consumer DJs who might be trying out DJing at home, whereas Serato is for professional DJs. [] said they are “different markets for sure”.⁸⁴

71.2. [] told us that mobile apps are not an alternative to professional DJ software but are present in the consumer space because there are a lot more younger people in that space who are more comfortable with mobiles.⁸⁵ [] said mobile apps are getting better and better, however they are more “at the surface” level whereas laptop applications go deeper and allow the user to do more.⁸⁶ [] also said it views mobile apps as a training ground, and introduction to the market.⁸⁷

71.3. [] told us that mobile apps are not seen as for professionals but would be good for entry level customers.⁸⁸ [] told us it sees mobile apps used more by beginner DJs rather than professionals. It also said it was not sure whether app usage is growing among DJs.⁸⁹

71.4. [] told us that the less professional a DJ is, the more likely they are to use a mobile app. It also said it competes with mobile app providers in terms of new customers only.⁹⁰ It said that it has seen that while it might initially lose new customers to a mobile app provider, in time and once these customers are ready to pay for DJ software, they come to []. [] said it estimates that almost the entirety of Algoriddim’s market is people who are DJing for the first time and trying it on their tablet because it is easier.⁹¹

71.5. We also received feedback from DJs on whether they would find mobile apps as an alternative to laptop applications. As a general note, in consumer facing markets it is not possible to survey all consumers nor in some cases a truly representative sample of them. We have therefore treated our interviews with DJs with caution and see them as providing corroborating evidence rather than conclusive evidence. One DJ told us it would “absolutely not” be an option to DJ using a mobile phone for a corporate gig.⁹² Another DJ told us that while connecting a mobile phone or tablet to a piece of DJ hardware

⁸³ [].

⁸⁴ Commerce Commission interview with [].

⁸⁵ Commerce Commission interview with [].

⁸⁶ Commerce Commission interview with [].

⁸⁷ Commerce Commission interview with [].

⁸⁸ Commerce Commission interview with [].

⁸⁹ Commerce Commission interview with [].

⁹⁰ Commerce Commission interview with [].

⁹¹ Commerce Commission interview with [].

⁹² Commerce Commission interview with [].

would be “fine” and potentially an option if something went wrong with the piece of hardware, it would never be preferential to DJ that way.⁹³

71.6. The Parties submitted that some professional DJs have had success using mobile apps to perform with and win competitions, in particular K Swizz.⁹⁴ In support of this, one DJ noted that K Swizz had won the 2022 DMCs World Championship using a mobile app, and said that using a mobile phone wouldn’t “hold you back”.⁹⁵ However, K Swizz appears to have switched to a laptop for the 2023 DMC World Championships.⁹⁶ We also understand that []⁹⁷

72. Consistent with mobile apps being targeted at beginners is that the pieces of DJ hardware that are bundled with mobile apps tend to have fewer features, and according to ATC, []⁹⁸ This suggests that mobile apps are unlikely to be an option to switch to for more experienced DJs with more expensive hardware. These DJs may not wish to switch to a less feature rich piece of hardware in order to use a mobile app.

73. The Parties submitted that the growth in mobile apps is coming from younger DJs rather than beginners.⁹⁹ Even if mobile apps are attractive to younger DJs, or the ‘next generation’ of DJs, and not just beginners, this still suggests that mobile apps may be targeted at a different customer set to the Parties’ (whose software may be aimed at more experienced DJs, and for use with DJ hardware).¹⁰⁰

74. ATC submitted that []¹⁰¹ []

⁹³ Commerce Commission interview with [] .

⁹⁴ K Swizz is a New Zealand DJ who won the 2022 DMC World DJ Championship using Algoriddim’s mobile app. ATC “Submission by AlphaTheta Corporation on Statement of Issues” (8 April 2024) at FN49 and Serato “Submission in response to Commerce Commission Statement of Issues” (8 April 2024) at [18].

⁹⁵ Commerce Commission interview with [] .

⁹⁶ “K-SWIZZ (New Zealand): 2023 Technics DMC World Championship Winning Routine” YouTube uploaded by DMC World (3 November 2023) <www.youtube.com>.

⁹⁷ inMusic “inMusic’s Response to Serato Audio Research Limited’s Submission in Support of AlphaTheta Corporation’s Clearance Application to Acquire Serato” (22 November 2023) at IV(d)(ii)(2).

⁹⁸ The ATC controllers that are compatible with mobile apps [] and [] include the DDJ-200 and DDJ-400. These are (in ATC’s words) [] DJ controllers (ATC RFI response (6 June 2024)).

⁹⁹ Although an internal document suggests that []

].

¹⁰⁰ One DJ we spoke with that uses Serato said that he would “maybe” like to see Serato develop a mobile app, but would rather Serato put its time and energy into laptop software (Commerce Commission interview with []). Another DJ told us that Serato creating a mobile app “doesn’t really interest” him (Commerce Commission interview with []). [] believed that no one mixing on a desktop wants an app (Commerce Commission interview with []).

¹⁰¹ Email from ATC with comments on unredacted SoUI (20 June 2024).

].¹⁰²

75. ATC submitted that a [

].¹⁰³ We do not consider this necessarily implies that mobile apps belong in the relevant market.

75.1. If consumers are upgrading from a mobile app to a laptop application, this may suggest that the products are not substitutes. Such behaviour may indicate that consumers view mobile apps as entry-level software but do not consider them a good alternative once they have made the decision to financially invest in, and sufficiently commit to, the hobby.¹⁰⁴

75.2. The evidence on upgrading focuses on the extent of switching from mobile apps to laptop applications. The relevant question for determining whether mobile apps should be included in the relevant market is, however, whether sufficient consumers would switch from laptop applications to mobile apps to defeat a SSNIP on laptop applications. For the constraint from mobile apps to be meaningful, we would need to see evidence of the latter. We are not satisfied the evidence shows this has occurred.

The evidence does not show that mobile apps impose a strong constraint on laptop applications

76. We agree with Serato that audiences may be indifferent to the DJ set up used and are not seeking a “laptop DJ”. However, we do not consider this to be relevant to the question of whether the customers in this market (that is, DJs using laptop applications) would switch sufficient purchases to alternatives. Audiences are not DJ customers, and it is not their choice that is relevant for the purposes of assessing substitutability.

77. We also recognise that – as Serato submitted – there are different ways to DJ (such as using vinyl, CDJs, laptops and mobiles/tablets). However, the main overlap between the merging parties occurs for DJ software (specifically laptop applications) and, as set out above, that has been the starting point for our assessment. The appropriate question to ask is whether customers of laptop applications would switch to alternatives (such as mobile apps) in response to a SSNIP in the price of laptop applications. We are not satisfied a sufficient number of customers would switch in response to a SSNIP on the price of laptop applications to justify broadening the relevant market to include to include mobile applications. Further,

¹⁰² ATC RFI response (6 June 2024) at p. 3.

¹⁰³ Email from ATC with comments on unredacted SoUI (20 June 2024).

¹⁰⁴ For example, [] told us that it is “constantly” losing customers who are upgrading from consumer to professional DJ hardware devices, since its software is not fully compatible with popular professional DJ hardware devices []. [] also stated that initially it was afraid of Algoriddim but then saw that once someone is prepared to pay for DJ software, they would come to []. [] said it doesn’t mind losing entry-level DJs to Algoriddim because it gets the lucrative part when the DJ is ready to pay money. Commerce Commission interview with [].

there is no indication that the constraint from mobile apps will significantly increase in the future such that they are likely to comprise part of the relevant market in the timeframe relevant to our assessment of the Proposed Acquisition.

78. Mobile apps and DJing on a smartphone or tablet are not new developments. Algoriddim was founded in 2006,¹⁰⁵ and other mobile apps CrossDJ and edjing were both released in 2012.¹⁰⁶ Even if we accept that the early iterations of mobile apps may have been fairly limited in terms of functionality and features, DJs have now had the ability to DJ using their mobile phone or tablet for over 10 years. If the evidence showed the growth of mobile apps has impacted on the growth of the Parties' laptop application software or their respective revenues, it would suggest that customers are substituting from laptop applications to mobile apps. However, we have not seen evidence or any indication that this has occurred or is likely to occur in the future.¹⁰⁷ This is despite mobile apps appearing to be much cheaper than laptop applications.¹⁰⁸

78.1. Serato, which does not have a mobile app, is []¹⁰⁹ [

]. ATC submitted that Serato [

].¹¹⁰ Be that as it may, the data does not provide evidence that mobile apps are a constraint.

78.2. The following graph provided by ATC shows that the number of rekordbox's laptop application users are [

]. The data instead

¹⁰⁵ <https://www.algoriddim.com/company>.

¹⁰⁶ The Application, at [6.18] and <http://world.edjing.com/about>.

¹⁰⁷ ATC submitted that the growth of laptop applications would have been even higher without mobile apps (ATC "Submission by AlphaTheta Corporation on the Statement of Issues" (8 April 2024) at [4.44]-[4.47]). While this may be true, we have not been provided any evidence to show this.

¹⁰⁸ For example, as at 12 August 2024, rekordbox mobile (at NZD\$12.99 monthly or NZD\$89.99 annually) is around half the price of rekordbox Core (at around NZD\$20 monthly or NZD\$200 annually). The price of rekordbox mobile is available within the app and price of rekordbox Core available here: <https://rekordbox.com/en/plan/>". The price of rekordbox Core was converted from USD\$12 monthly and USD\$120 annually at an exchange rate of 1.67.

¹⁰⁹ [].

¹¹⁰ Email from ATC with comments on unredacted SoUI (20 June 2024).

seems consistent with the other evidence showing mobile apps are targeted at different customers and are reaching new users rather than impacting on the growth of laptop application customers.

Figure 1: rekordbox monthly average users over time

[

]

Source: ATC "Submission by AlphaTheta Corporation on the Statement of Issues" (8 April 2024) at [6.7(c)].

78.3. Other market participants did not indicate that the growth of mobile apps had negatively affected growth in the numbers of their laptop application users.

78.3.1. [] told us it was not sure how much the rise of Algoriddim had impacted its sales (and believed any impact would be small) but noted that it did impact the number of its downloads for free users.¹¹¹ It said if Algoriddim did not exist its user numbers would probably be a little bit higher, but that Algoriddim’s existence has not been “catastrophic”.¹¹²

78.3.2. [] told us it was difficult to say if there had been an impact on its software sales due to the rise of mobile apps, partly because its customer base is mature users and it is younger customers who are using mobile apps.¹¹³

79. We have also seen limited evidence that mobile apps have impacted the decision making of DJ software providers. If mobile apps are a competitive constraint on laptop applications as the Parties have argued, we might have expected those suppliers to invest in developing a mobile app. Only ATC appears to have done so,

¹¹¹ Commerce Commission interview with [].

¹¹² Commerce Commission interview with [].

¹¹³ Commerce Commission interview with [].

although the internal documents indicate that [].

79.1. [

].¹¹⁴ [

].^{115 116} [

].

79.2. ATC submitted that the competitive threat posed by mobile apps on laptop applications led to it launching a new version of its rekordbox mobile app in 2023 that included performance functionality.¹¹⁷ However, the internal documents indicate that the [].

79.3. [

] – it also noted that customers are not “screaming out for apps”.¹¹⁸ [] also said the bigger threat to laptop applications is embedded software, rather than mobile apps, and considered that the trend towards customers using mobile apps is “not clear”.¹¹⁹

79.4. [] told us it developed a mobile app five years ago that it did not release as it was not satisfied with the quality. It did not tell us of any plans to develop a mobile app and told us that the mobile app market is “not so lucrative”.¹²⁰

80. The Parties submitted that mobile apps have competed with laptop applications through innovation. We accept Algoriddim has contributed to advancements within the DJ software industry, but we consider that it seems mainly Algoriddim itself, rather than mobile apps as a category, that is driving this innovation.¹²¹ For example, an internal document from Serato refers to []¹²² and [

].¹²³ We did not see

evidence of innovations from other mobile app providers and, as noted above, we consider that mobile apps tend to have fewer features than laptop applications.

¹¹⁴ [].

¹¹⁵ [].

¹¹⁶ Another internal document from Serato states [

].

¹¹⁷ ATC “Submission by AlphaTheta Corporation on the Statement of Issues” (8 April 2024) at [4.11].

¹¹⁸ Commerce Commission interview with [].

¹¹⁹ Commerce Commission interview with [].

¹²⁰ Commerce Commission interview with [].

¹²¹ We also note that Algoriddim is not purely a mobile app provider – it also has a laptop application.

¹²² [].

¹²³ ATC supports this argument (see ATC “Confidential submission on Confidential Sol” (9 April 2024) at [1]).

Supply side substitution is not sufficient to expand the product market beyond laptop applications

81. We are not satisfied that supply side substitution is sufficiently strong to expand the relevant product market to include mobile apps.

81.1. First, supply side substitution requires that a firm can quickly switch production to the product in question with little or no investment.¹²⁴ We do not consider the evidence suggests switching between developing laptop applications and mobile apps meets that standard. Developing a laptop application requires writing to a different platform than that used to develop a mobile app. This implies additional investment would be required to switch. For example, ATC stated that it has [] development staff dedicated to its rekordbox mobile app and is spending [] annually on research and development.¹²⁵

81.2. Second, the examples that ATC provided are where a producer of a laptop application has developed a mobile app. However, the relevant question for supply side substitution in this matter is whether mobile app providers can switch to producing laptop applications in response to SSNIP for laptop applications. The relevant examples would therefore be where mobile app producers have developed laptop applications quickly and without significant cost in response to a price increase for laptop applications. We have not been provided with such examples.

Music production software and embedded software are not viable substitutes for laptop applications

82. We do not consider that music production software (ie, software that is used to create music) and embedded software are sufficiently close substitutes for laptop applications to be included in the product market.

82.1. While some DJs may use music production software to DJ, we have not seen any evidence to suggest that it is a sufficiently close substitute for laptop applications to justify including in the relevant product market. For example, even though (as ATC noted)¹²⁶ the 2024 Digital DJ Tips Global Census results show around 20% of DJs are regularly producing music and that many appeared to own music production software, music production software did not appear in the chart “What software do you use to DJ?”.¹²⁷ We have not seen any evidence to suggest DJs view music production software as a good alternative to DJ software (we discuss this further at paragraphs [173]-[175]).

¹²⁴ Mergers and Acquisitions Guidelines above n3 at [3.16].

¹²⁵ ATC “Submission by AlphaTheta Corporation on the Statement of Issues” (8 April 2024) at [4.11(b)].

¹²⁶ ATC “Submission by AlphaTheta Corporation on the Statement of Issues” (8 April 2024) at [5.9].

¹²⁷ Digital DJ Tips “Global DJ Census 2024” <https://www.digitaldjtips.com/census-results-2024/>. The chart is reproduced at paragraph [136] below.

- 82.2. We also do not consider the evidence provided by the Parties to support embedded software belonging in the relevant market to be persuasive. Embedded software is used to operate DJ hardware such as all-in-ones and DJ players. It can only be used on the DJ hardware in which it is embedded. To use embedded software, a DJ would need to purchase new hardware and operate a different set-up (for example an all-in-one or DJ player with mixer). It is unlikely that a SSNIP on DJ software would result in DJs switching to all-in-ones and DJ players given they are much more expensive in price (see FN131).

Geographic market

83. ATC submitted that the supply of DJ hardware and DJ software takes place on a global basis, however for the purposes of its assessment of the Proposed Acquisition in the Application it has focused on a national market (New Zealand).¹²⁸ We agree with this approach.

Conclusion on the DJ software market

84. We consider the relevant market for assessing the Proposed Acquisition is the national market for the supply of DJ software (the DJ software market). We are:
- 84.1. satisfied that laptop applications are likely to impose such a constraint on the merged entity that they form part of the relevant market; but
 - 84.2. not satisfied that mobile apps, music production software and embedded software are likely to impose a significant constraint of the merged entity, and therefore consider that they do not form part of the relevant market.
85. We recognise there is not a clear distinction between competition for laptop applications and mobile apps. There are likely to be some DJs who view laptop applications and mobile apps as substitutable. For example, some DJs who use entry-level controllers may place a relatively high value on the portability of mobile devices and so see mobile apps as a good alternative to laptop applications. We further recognise that the products in question display some dynamic elements, such that substitution may change over time. For example, over time new forms of DJing have emerged and suppliers of DJ hardware and software have responded through launching new products. This means that, in time, the nature of substitution between laptop applications and mobile apps may change. However, despite this, we are not satisfied that mobile apps are a sufficiently close substitute to laptop applications to justify including them the relevant DJ software market. Furthermore, we are not satisfied that market conditions will change to such in the period relevant to our assessment (we consider the appropriate period for assessing the effects of

¹²⁸ The Application at [5.29]-[5.30].

the Proposed Acquisition on competition is over the next 1-2 years),¹²⁹ that we would reach a different view on the boundaries of relevant DJ software market.

86. The above said, our overall assessment of the Proposed Acquisition does not hinge on whether mobile apps are part of the relevant market or not. What matters is the extent of constraint from all sources, including mobile app suppliers that would be imposed on the merged entity. As such, we consider the constraint from mobile app suppliers in our competition assessment sections.

The DJ hardware market

ATC's views

87. ATC submitted that the relevant market is the supply of DJ hardware because:¹³⁰
- 87.1. many categories of DJ hardware are substitutable (such as a DJ players, all-in-one systems and controllers); and
 - 87.2. the technological difference between the different categories is becoming smaller.

Our assessment of the DJ hardware market

88. ATC is a major supplier of DJ hardware, but as Serato does not supply DJ hardware there is no competitive overlap between the Parties in this area. However, DJ hardware is used with DJ software and therefore the potential for vertical effects arises. For this reason, we have assessed the relevant market for DJ hardware.
89. DJ software is primarily used with controllers and, as such, this is our starting point for market definition.
- 89.1. On the demand side, there may be some limits to the extent to which DJs would be willing to switch from controllers to other types of DJ hardware. For example:
 - 89.1.1. DJ players are generally more expensive than controllers and require a separate mixer.¹³¹ Controllers are more portable than a DJ player/mixer setup.¹³² DJ players require a different style of DJing, where the DJ needs to prepare music in advance which gets

¹²⁹ We also assess competition over a period of greater than five years in our assessment of vertical effects to reflect the period that the SPA provisions provide protections to the vendor (see paragraphs [273]-[280] below).

¹³⁰ The Application at [5.22].

¹³¹ For example, currently at Mix Foundation (a New Zealand music retailer) the prices for Pioneer controllers range from NZD\$400 to NZD\$3500, whereas the price for Pioneer DJ DJ players (of which two are required) range from NZD\$1,500 to NZD\$5,000. It would also be necessary to buy a mixer, which for a Pioneer DJ mixer range from NZD\$749-\$6,500. See Mix Foundation < www.mixfoundation.co.nz > available 29 July 2024.

¹³² See for example DJ City "DJ Controller VS Turntables VS CDJs – Which Setup Is Best?" <www.djcity.com.au> (4 October 2021).

downloaded to a USB.¹³³ [] did not consider its controllers competed closely with DJ players.¹³⁴

89.1.2. All-in-one systems combine DJ players and mixers into a single unit. They are more portable than a DJ player/mixer set up but more expensive than controllers.¹³⁵ Despite the cost, some customers that use controllers may view all-in-one systems as substitutable due to their portability and because they can be used as a controller with a connected device.

89.2. On the supply side, existing manufacturers of controllers may have the technical knowledge to build DJ players although it is unclear if it would be straightforward to enter the market to supply them.¹³⁶ [] believed it may be difficult to enter the market given Pioneer DJ's existing position in the market.¹³⁷ [] considered it would take a lot of development to make a DJ player.¹³⁸ [] claimed that inMusic had attempted to compete with Pioneer DJ but had limited success.¹³⁹

90. For the purposes of our analysis, we assess the Proposed Acquisition on a product market that includes controllers and all-in-ones but excludes DJ players and other types of DJ hardware (which we refer to as “the DJ hardware market”). That said, we do not think that the precise boundaries of the market affects our assessment. For example, the main reason we have defined the DJ hardware market is to assess potential vertical effects from the Proposed Acquisition. Whether or not one includes DJ players and mixers in the DJ hardware market will not affect the potential harm to competition for the supply of controllers due to vertical effects that we identify below.

With and without scenarios

91. To assess whether a merger is likely to substantially lessen competition in a market, we compare the likely state of competition if the Proposed Acquisition proceeds (the scenario with the merger, often referred to as the factual) with the likely state of competition if it does not (the scenario without the merger, often referred to as the counterfactual).

Our approach to deciding what is likely without the Proposed Acquisition

92. As noted by the High Court in *Woolworths*, the Commission is required to consider each of the counterfactuals that are real and substantial prospects. A relevant

¹³³ See for example DJ Tech Reviews “CDJs vs DJ Controllers (Which is best)” <www.djtechreviews.com>.

¹³⁴ Commerce Commission interview with [].

¹³⁵ For example, currently at Mix Foundation the prices for Pioneer DJ all-in-one controllers range from NZD\$2,300 to NZD\$6,300. See Mix Foundation <www.mixfoundation.co.nz> available 29 July 2024.

¹³⁶ For example [] said it could build a DJ player with its existing knowledge. Commerce Commission interview with [].

¹³⁷ Commerce Commission interview with [].

¹³⁸ Commerce Commission interview with [].

¹³⁹ Commerce Commission interviews with [] and [].

counterfactual involves more than a possibility, but the effect does not need to be “more likely than not”.¹⁴⁰

93. We do not choose a counterfactual that we consider has the greatest prospects of occurring (ie, is the ‘most likely’). Rather, a likely counterfactual is something that has a real chance of occurring.¹⁴¹
94. As a practical matter, we usually focus our analysis on the likely counterfactual we consider is the most competitive. If we are not satisfied that competition would not be likely to be substantially lessened when that counterfactual is compared to the factual, we must decline clearance.¹⁴²
95. We make a pragmatic and commercial assessment of what is likely to occur in the future without the merger. This assessment is based on the information we obtain through our investigation and takes into account factors including market growth and technological changes.
96. Often the best guide of what would happen without a merger is what is currently happening (ie, the status quo). However, where a market is likely to undergo changes that will affect competition in the counterfactual, we take these changes into account.¹⁴³

With the acquisition

97. With the acquisition, ATC would own 100% of the shares of Serato. ATC submitted that it intends for Serato to continue to operate as a separate business based in New Zealand.¹⁴⁴
98. ATC submitted that the terms of the sale and purchase agreement it has entered into with Serato in relation to the Proposed Acquisition (the SPA) preclude ATC from refusing to allow Serato to partner with other DJ hardware providers or making Serato’s DJ software less attractive for the providers to partner with.¹⁴⁵
99. The Parties submitted that these clauses (which end 31 December 2028) should be taken into account when considering the competition impact of the Proposed Acquisition and that it is appropriate for the Commission to consider them as forming part of the with-the-merger scenario.¹⁴⁶
100. The purchase price for Serato is made up of an upfront payment and [] contingent payments to be made to the sellers of Serato (the Sellers) based on Serato’s financial performance [

].¹⁴⁷ As a result, the SPA contains several post-

¹⁴⁰ *Woolworths & Ors v Commerce Commission* (HC) above n8 at [111].

¹⁴¹ *Woolworths & Ors v Commerce Commission* (HC) above n8 at [111].

¹⁴² Mergers and Acquisitions Guidelines above n3 at [2.33]-[2.34].

¹⁴³ Mergers and Acquisitions Guidelines above n3 at [2.36].

¹⁴⁴ The Application at [1.3].

¹⁴⁵ The Application at [1.5(c)].

¹⁴⁶ The Application at [7.23].

¹⁴⁷ The Application at [3.2].

completion obligations on ATC that are designed to prevent ATC from making changes to the Serato business that could adversely affect the earnout.¹⁴⁸

101. The main obligations on ATC relevant for the purposes of our analysis are:¹⁴⁹

101.1. [ATC] undertakes to the Sellers that it will, during the Contingent Consideration Period, act in good faith and, using all reasonable endeavours, support the growth of and operate and manage [Serato] with a view to maximising the [relevant profit metric]" (clause 6.1, Schedule 11);

101.2. "[ATC] will ensure that [Serato] is managed in a prudent manner consistent with the 12 months immediately prior to Completion" (clause 6.2.1, Schedule 11); and

101.3. "[ATC] will ensure that [Serato] does not (without the prior written consent of the Sellers' Representative)...materially change the nature or scope of its Business as presently conducted..." (clause 6.2.9(a), Schedule 11).

102. For reasons we discuss below at paragraphs [223]-[224], while we have taken these clauses into account as part of the factual, we are not satisfied they will prevent a substantial lessening of competition occurring in the relevant markets over time.

Without the acquisition

103. ATC submitted that, absent it acquiring Serato, it is likely that Serato would be []¹⁵⁰ ATC said that in the counterfactual, Serato will continue to operate as it does currently [] and ATC will continue to partner with Serato as it has done for over 10 years.¹⁵¹

104. We consider that the relevant counterfactual is one in which Serato would remain as an independent competitor, either under third party ownership or as a standalone entity.

How the merger could substantially lessen competition

105. We have considered three possible ways in which the merger would have, or would be likely to have, the effect of substantially lessening competition:

105.1. first, the merger could have unilateral effects in the supply of DJ software;

105.2. second, the merger could have vertical effects in the supply of DJ hardware, by providing the merged entity with the ability and incentive to foreclose competitors in the DJ hardware market (as part of our discussion on vertical

¹⁴⁸ ATC "Submission by AlphaTheta Corporation on the Statement of Issues" (8 April 2024) at [7.11].

¹⁴⁹ ATC "Submission by AlphaTheta Corporation on the Statement of Issues" (8 April 2024) at [7.19].

¹⁵⁰ The Application at [3.11].

¹⁵¹ The Application at [3.12].

effects we also discuss the possibility for vertical effects to arise in the supply of DJ software); and

- 105.3. third, the merger could substantially lessen competition through the merged entity's access to its competitors' commercially sensitive information that it would obtain post-acquisition through the integration process of their DJ hardware with Serato software.

Competition analysis – unilateral effects

106. Unilateral effects can arise when a firm acquires a competitor that would otherwise provide a significant competitive constraint. Such effects occur when the merged firm can profitably increase price above the level, or reduce quality below the level, that would prevail without the acquisition, without being thwarted by demand side substitution or rival firms' competitive responses.¹⁵²
107. In assessing whether unilateral effects are likely to arise from the Proposed Acquisition, we considered:
- 107.1. closeness of competition: the degree of constraint the Parties impose upon one another in the market for DJ software;
- 107.2. remaining competitive constraints: the degree of constraint that existing competitors would impose on the merged entity; and
- 107.3. entry and expansion: how easily competitors could enter and/or expand.¹⁵³
108. We are not satisfied that the merger will not have, or would not be likely to have, the effect of substantially lessening competition in the DJ software market due to unilateral effects. Based on the evidence before us, we consider it is likely that the Proposed Acquisition will give the merged entity the ability to profitably increase the prices of and/or reduce the quality of its DJ software products that would prevail without the merger. As we explain below the main reasons are:
- 108.1. the Parties compete closely and the Proposed Acquisition would eliminate that competition;
- 108.2. the remaining DJ software competitors are either significantly smaller or have products that are viewed as being for beginner DJs, or both; and

¹⁵² For simplicity, when we refer to concerns that the acquisition may result in an increase in price, this also includes the possibility that the impact of the acquisition is a reduction in quality or some combination of a price and quality effect.

¹⁵³ Another potential constraint on a merged entity is countervailing power. Countervailing power exists when a customer possesses special characteristics that give the customer the ability to substantially influence the price the merged entity charges (Mergers and Acquisitions Guidelines above n3 at [3.113]-[3.117]). For example, customers may have countervailing power if they are able to self-supply or can sponsor new entry. However, given the ultimate customers are individual DJs, we did not consider that they would have any significant countervailing power (for example, individual customers are unable to sponsor new entry).

108.3. there are high barriers to entry and expansion.

Closeness of competition between the Parties

109. To determine whether the Proposed Acquisition would be likely to result in a substantial lessening of competition in the supply of DJ software due to unilateral effects, we first looked at the extent to which the Parties compete against each other. This enables us to determine what competition is ‘lost’ with the Proposed Acquisition and would therefore need to be sufficiently ‘replaced’ with other constraints, discussed further below, in order for the Commission to be satisfied that the Proposed Acquisition does not substantially lessen competition.

Competition between the Parties

ATC’s views

110. ATC submitted that rekordbox and Serato are not each other’s closest competitor as the two have.¹⁵⁴

110.1. different histories (rekordbox started as a library management tool and then developed into performance software, while Serato started as performance software); and

110.2. different users (Serato is predominantly used by “scratch” DJs while rekordbox is primarily used by house/techno DJs).¹⁵⁵

111. ATC told us [

[]^{156 157}
].¹⁵⁸

112. ATC submitted that [

].¹⁵⁹ According to ATC:

112.1. [

¹⁵⁴ ATC “Submission by AlphaTheta Corporation on the Statement of Issues” (8 April 2024) at [6.7].
¹⁵⁵ “Scratch” DJs move a record back and forth on a turntable to produce different sounds. This type of DJing is typically associated with hip hop music. House/techno music are genres of electronic dance music.
¹⁵⁶ ATC RFI response (6 June 2024) p. 10.
¹⁵⁷ []
¹⁵⁸ ATC RFI response (6 June 2024) p. 3.
¹⁵⁹ ATC RFI response (6 June 2024) pp. 2-4.

112.2.

112.3.

].

113. ATC []:¹⁶⁰

113.1. [

113.2.

113.3.

113.4.

113.5.

].

114. ATC also submitted that the SPA provisions and earnout mechanism will ensure that the Parties are incentivised to continue to compete until at least 31 December 2028, which is when those provisions expire.¹⁶¹

Serato's views

115. Serato submitted that rekordbox and Serato have different customer bases and target markets. Serato compared the two as follows:¹⁶²

115.1. Serato has a presence primarily [

].

¹⁶⁰ ATC RFI response (6 June 2024) p. 3.

¹⁶¹ ATC "Submission by AlphaTheta Corporation on the Statement of Issues" (8 April 2024) at [6.9].

¹⁶² Serato "Submission in response to Commerce Commission Statement of Issues" (8 April 2024) at [99].

115.2. rekordbox has a stronger brand recognition in []].

Serato also said many rekordbox users like rekordbox's preparation feature, which allows users to organise playlists and export music to a USB drive for use on Pioneer DJ CDJs or other embedded hardware.

116. Serato submitted that the competition between Serato and rekordbox is not particularly strong as, in its view, rekordbox []].¹⁶³ In support of this, Serato submitted that ATC's history of innovation in the DJ hardware space is []].¹⁶⁴

117. It further submitted that the []].¹⁶⁵ and that rekordbox's market position reflects ATC's success as a DJ hardware provider.¹⁶⁶ Serato said it is therefore more influenced by Algoriddim, VirtualDJ and Traktor.¹⁶⁷

118. Serato also submitted that the earnout mechanism in the SPA inherently supports competition continuing between the Parties post-acquisition, although Serato said it does not consider it necessary to rely on this point.¹⁶⁸

Our assessment of how closely the Parties compete for DJ software

119. The evidence we gathered strongly indicates that Serato and rekordbox compete closely for the supply of DJ software.

120. []].

].

121. Internal documents from Serato stated:

121.1. []].

];¹⁶⁹

¹⁶³ Serato "Submission in response to Commerce Commission Statement of Issues" (8 April 2024) at [80].

¹⁶⁴ Serato "Submission in response to Commerce Commission Statement of Issues" (8 April 2024) at [89], [92] and [94].

¹⁶⁵ Serato "Submission in response to Commerce Commission Statement of Issues" (8 April 2024) at [89].

¹⁶⁶ Serato "Submission in response to Commerce Commission Statement of Issues" (8 April 2024) at [96].

¹⁶⁷ Serato "Submission in response to Commerce Commission Statement of Issues" (8 April 2024) at [80].

¹⁶⁸ Serato "Submission in response to Commerce Commission Statement of Issues" (8 April 2024) at [100].

¹⁶⁹ []].

121.2. [

];¹⁷⁰

121.3. [

];¹⁷¹

121.4. Serato and rekordbox [

];¹⁷²

121.5. [

];¹⁷³

121.6. [

];¹⁷⁴ and

121.7. [

].¹⁷⁵

122. Internal documents from ATC stated:

122.1. [

];¹⁷⁶ and

122.2. [

].¹⁷⁷

¹⁷⁰ [].
¹⁷¹ []

].
¹⁷² [].
¹⁷³ [].
¹⁷⁴ [].
¹⁷⁵ [].
¹⁷⁶ [].
¹⁷⁷ [].

123. While some market participants told us that Serato and rekordbox have different uses,¹⁷⁸ overall the evidence suggests that the two have broadly similar software offerings:

123.1. DJs can use both Serato and rekordbox for performance and preparation.¹⁷⁹ While rekordbox was originally used for preparation, it has now had performance functionality for many years.

123.2. [

].

However, we do not consider this affects our conclusion that the Parties are close competitors.

123.2.1. [

123.2.2.

].¹⁸⁰

123.3. The Parties' software products appear to be the only software that is positioned as being for professional DJs. For example, in its report in support of the Application, NERA, an economic consulting firm, submitted that Serato and rekordbox are closely positioned as they have a similar pricing structure

¹⁷⁸ Commerce Commission interviews with [] and [].

¹⁷⁹ [

].

¹⁸⁰ For example, [

] (ATC RFI response (6 June 2024) at p. 3).

and both appear to be positioned as “premium” products¹⁸¹ and [] told us that while Serato is the number one software for professional DJs, rekordbox also serves the professional market.¹⁸²

124. Although the Parties submitted that Serato and rekordbox are more suited for DJing with different types of music, we do not consider that any differentiation in this area is such that they are not close competitors:

124.1. While [] told us that Serato is more used by hip hop or open format DJs, it still considers that the two compete, and that this competition drives innovation within the industry.¹⁸³

124.2. [] told us Serato is not more suited to one type of music than rekordbox, and that he has DJed drum and bass, house and electronic music (which the Parties argued is more suited to rekordbox) on Serato for nearly 14 years.¹⁸⁴

124.3. [] told us that the DJ hardware and software a DJ uses is not determined by the music they are mixing.¹⁸⁵

124.4. ATC’s submission references the results of a survey it conducted, which found that while [] of rekordbox users said they play house/techno music, [] of respondents also said they usually played hip hop music (which the Parties argued is more suited to Serato) (more than one answer was able to be given).¹⁸⁶

124.5. An internal document from Serato looked at []¹⁸⁷

125. The evidence gathered during our investigation suggests that Serato is generally viewed in terms that rekordbox is not (such as a market leader and ‘industry standard’).¹⁸⁸ Despite this, the evidence we received suggested that rekordbox (rather than other laptop applications) is the next best alternative for Serato customers:

¹⁸¹ NERA Economic Consulting “AlphaTheta Corporation/Serato: unilateral effects and foreclosure theories of harm” (27 November 2023) at [71].

¹⁸² Commerce Commission interview with [].

¹⁸³ [] told us that the competition pushes the other to come up with something new and gave the example of Serato implementing a new feature and then rekordbox later adding a version of that feature that wasn’t as good (Commerce Commission interview with []).

¹⁸⁴ Commerce Commission interview with [].

¹⁸⁵ Commerce Commission interview with [].

¹⁸⁶ ATC “Submission by AlphaTheta Corporation on the Statement of Issues” (8 April 2024) at FN 70.

¹⁸⁷ [].

¹⁸⁸ Commerce Commission interviews with [], [], [], [] and [].

- 125.1. [] told us that most of its customers are using either Serato or rekordbox;¹⁸⁹
- 125.2. [] told us that if Serato was unavailable, people would use rekordbox. He also said both types of software allow users to locate, organise, store and select music;¹⁹⁰
- 125.3. [] told us that if someone was using Serato, they would probably see rekordbox as their next best alternative;¹⁹¹
- 125.4. [] said if they were not using Serato, they would use rekordbox;¹⁹² and
- 125.5. [] told us that the most popular DJ software is Serato, rekordbox and djay, and that rekordbox is now a competitor to Serato's DJ software.¹⁹³
126. The Parties are likely to be in competition to secure a large proportion of laptop application customers. [

].

127. Due to the popularity of ATC's Pioneer DJ hardware (we estimate Pioneer DJ supplies around [] of the DJ hardware market), Serato and rekordbox are likely to be in competition to secure software users among a large proportion of the DJ population. ATC stated that []¹⁹⁴ rekordbox Free offers similar features to Serato's paid version, is fully integrated with Pioneer DJ hardware and is available free to around [] of Serato's potential customers. For these reasons it seems highly likely that Serato would view rekordbox as a strong competitive constraint.
128. Finally, although the Parties submitted that the SPA provisions would ensure that they would remain incentivised to compete with one another, we do not consider we can rely on those contractual provisions (that were designed to protect the earnout Serato hopes to receive) to ensure that competition in the industry would be ongoing. We set out the reasons why we are not satisfied we can rely on the SPA

¹⁸⁹ Commerce Commission interview with [].

¹⁹⁰ Commerce Commission interview with [].

¹⁹¹ Commerce Commission interview with [].

¹⁹² Commerce Commission interviews with [] and []. [] said that this decision was due to what he would be most likely to see in a venue (which would be Pioneer CDJs).

¹⁹³ Commerce Commission interview with [].

¹⁹⁴ ATC RFI response 6 June 2024 p. 3.

provisions further at paragraphs [223]-[224] below, as it is also relevant to our discussion of vertical effects.

Market shares

129. Although not determinative of whether a merger is likely to have the effect of substantially lessening competition, market shares and changes in market shares resulting from a merger can indicate the extent to which firms in a market are subject to competitive constraints, and the extent to which those constraints might change as a result of a merger.¹⁹⁵

ATC's views

130. In the Application, ATC submitted that the Parties' combined global market share is [].¹⁹⁶ ATC also submitted that any market share calculations need to include mobile app providers and other software providers like Cross DJ, PCDJ Dex3 and Future.dj Pro.¹⁹⁷

Serato's views

131. Serato submitted that revenue figures are not a reliable source for market shares (given these figures don't take into account free DJ software and because revenue earned from a product does not necessarily equate to a customer using that software, particularly if the hardware supports multiple kinds of software), and that monthly average user (MAU) data is a better indicator (although is still subject to limitations).¹⁹⁸

Our assessment

132. We disagree with the market share estimates ATC presented in the Application, primarily because ATC has included mobile app providers in these market share calculations. As discussed above at paragraphs [61-88], we have used a DJ software market that is limited to laptop applications, with mobile apps being treated as an out-of-market constraint (and therefore excluded from our market share calculations). We also believe that the other DJ software providers noted by ATC at paragraph [130] do not warrant inclusion in our market share calculations. None of these providers were cited as viable alternatives in any of our interviews with market participants.
133. We assessed market shares for DJ software using revenue provided by market participants. However, difficulties in assessing market shares may have resulted in the Parties' market shares being over- or underestimated. For example, the different strategies of the DJ software companies (where some make revenue supplying to

¹⁹⁵ Mergers and Acquisitions Guidelines above n3 at [3.48-49].

¹⁹⁶ The Application at [6.6].

¹⁹⁷ ATC "Confidential submission on Confidential Sol" (9 April 2024) at [4].

¹⁹⁸ Serato "Submission in response to Commerce Commission Statement of Issues" (8 April 2024) at [109]-[111].

consumers while others supply DJ software as part of a DJ hardware bundle) makes it harder to directly compare revenues. Some third parties did not provide us with full information, and we had to estimate some figures (including New Zealand revenue in some cases). As such, we consider that market share information is one part of the broader set of evidence.

134. With this in mind, our assessment of market shares shows that, when only laptop applications are considered, Serato is likely to be the leading supplier in New Zealand and rekordbox is also a commonly used DJ software product. The merged entity is likely to have a high market share in New Zealand (see Table 1):

Table 1: Estimates of DJ software market shares based on revenues¹⁹⁹

Party	New Zealand market share (%)	Global market share (%)
Serato	[
ATC (rekordbox)		
Merged entity		
Native Instruments (Traktor)		
Algoriddim (djay)		
inMusic		
VirtualDJ]
Total	100%	100%

135. The following MAU figures we collected also support Serato and rekordbox being two of the leading DJ software providers. The interview and document evidence set out earlier shows Serato and rekordbox as being close competitors for DJ software. The figures show rekordbox's MAU [] which would imply it is becoming an increasingly strong competitor to Serato. At the same time, the number of []. [] did not provide information to us and therefore we were not able to assess how their MAU figures were trending.

Figure 2: DJ software providers' New Zealand monthly average users

[

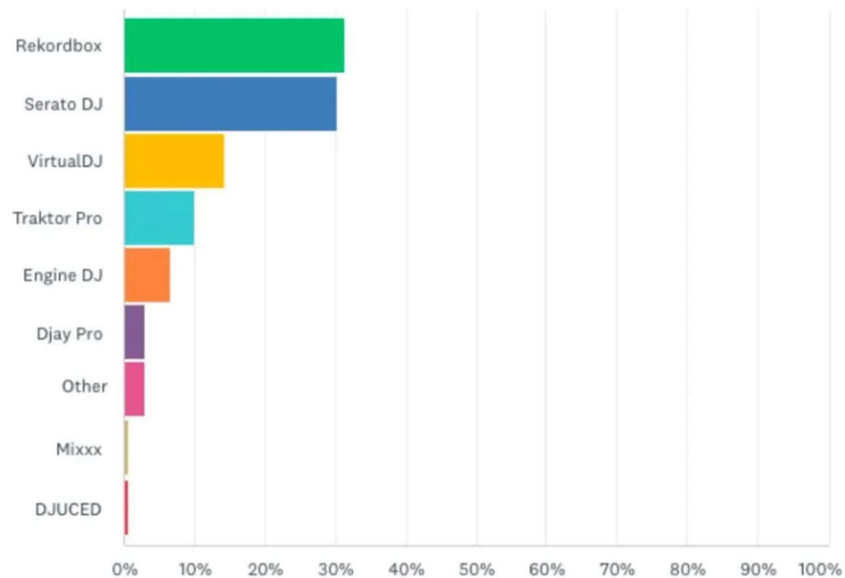
¹⁹⁹ Table 1, New Zealand market share (%) does not add to 100% due to rounding.

].

136. We also consider that information from the Digital DJ Tips Global Census is persuasive in showing that the Parties are two of the leading DJ software providers and compete closely. The census is a yearly survey of the opinions of DJs on topics such as the DJ software and DJ hardware they use. The Parties have consistently been the two most popular software products among the DJs surveyed from at least as far back as 2020, with the top software switching back and forth over the years between Serato and rekordbox:

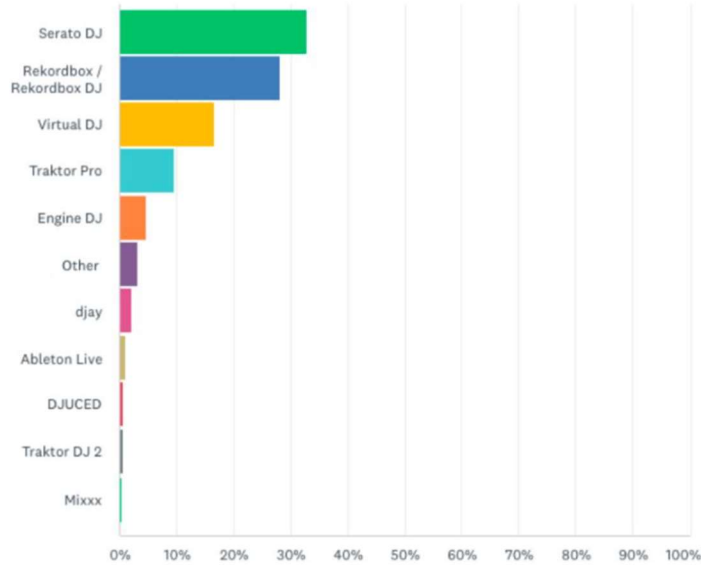
Figure 3: Digital DJ Tips Global DJ Census results

WHAT SOFTWARE DO YOU USE TO DJ?



Source: Digital DJ Tips Global DJ Census 2024

WHAT SOFTWARE DO YOU USE TO DJ?



Source: Digital DJ Tips Global DJ Census 2023

137. While the Parties both argued that this survey is not representative of the DJ industry (as the survey reflects older, more experienced DJs)²⁰⁰ we consider that it is a further piece of evidence in support of the Parties competing closely.

137.1. The Parties both [redacted], including in an [redacted],²⁰¹ and [redacted]²⁰² indicating that they might view it as a legitimate source of information.

137.2. Serato told us that its [redacted].²⁰³ [redacted].

138. However, as with our market share calculations, we recognise the limitations of the Census data. For example, we agree with the Parties that the survey may not be representative of all DJs (as approximately 45% of the DJs surveyed in 2024 are 45 or

²⁰⁰ ATC “Submission by AlphaTheta Corporation on the Statement of Issues” (8 April 2024) at [4.38]-[4.43] and Serato “Submission in response to Commerce Commission Statement of Issues” (8 April 2024) at [46].

²⁰¹ [redacted].

²⁰² [redacted]

[redacted]. [redacted].

²⁰³ Commerce Commission meeting with Serato and ATC (29 April 2024).

older, and approximately 33% are from the US). That said, we consider that it still may be representative of the Parties' core customer base.

139. We have therefore considered the survey information as a part of the broader set of evidence.

Conclusion on closeness of competition between Serato and rekordbox/ATC

140. In our view, Serato and rekordbox compete closely. Users of Serato and rekordbox are likely to benefit from the competitive constraint that the Parties impose upon one another in the supply of DJ software. The Proposed Acquisition would eliminate this constraint, as well as the constraint rekordbox would likely continue to impose on Serato as it grows.

Constraint from other competitors

Constraint from other laptop application and embedded software competitors

ATC's views

141. ATC submitted that, post-Acquisition, it will continue to be constrained by vigorous competition from other DJ software solutions (including mobile apps and laptop applications).²⁰⁴
142. ATC submitted that the DJ software industry is highly competitive, with a range of software providers (including inMusic, Native Instruments, VirtualDJ and Algoriddim) being well placed to continue to innovate and expand over the next five years.²⁰⁵
143. ATC also submitted that [] market share shows that it is Serato's closest competitor.²⁰⁶ ATC said []²⁰⁷
144. In its report in support of ATC's Application, NERA submitted that competing laptop software providers such as djay, Mixvibes, Traktor and VirtualDJ are likely to continue to provide constraint on the merged entity's pricing and quality.²⁰⁸ NERA also submitted that differentiation between laptop software providers is typically on pricing and rival providers would be able to re-price and re-position their products to compete with rekordbox/Serato.²⁰⁹

Serato's views

145. Serato submitted that competition from the "broad range" of other providers (such as VirtualDJ, Traktor, Engine DJ, Algoriddim, Mixxx and DJUCED) will provide strong

²⁰⁴ The Application at [6.1].

²⁰⁵ ATC "Submission by AlphaTheta Corporation on the Statement of Issues" (8 April 2024) at [6.12].

²⁰⁶ Email from ATC with comments on unredacted SoUI (20 June 2024).

²⁰⁷ Email from ATC with comments on unredacted SoUI (20 June 2024).

²⁰⁸ NERA Economic Consulting "AlphaTheta Corporation/Serato: unilateral effects and foreclosure theories of harm" (27 November 2023) at [60].

²⁰⁹ NERA Economic Consulting "AlphaTheta Corporation/Serato: unilateral effects and foreclosure theories of harm" (27 November 2023) at [83].

constraint post-acquisition that will be sufficient to prevent a substantial lessening of competition.²¹⁰

146. Serato also submitted that [

].²¹¹

147. Serato also submitted that DJ hardware partners are likely to provide a significant competitive constraint, noting that the importance of integrating their products with Serato says nothing about the strength of the competitive constraint other DJ software providers exert on Serato.²¹²

Our assessment

148. Post-acquisition, the main competitors to the merged entity would be VirtualDJ and Native Instruments' Traktor software (both of which are laptop applications), Algoriddim's djay (which is available as a laptop application and a mobile app) and inMusic's Engine DJ (which is available as a laptop application and as embedded software in inMusic hardware). We are not satisfied, based on the evidence before us, that competition from these competitors would sufficiently replace the competition that would be lost with the Proposed Acquisition.

149. We are not satisfied that existing laptop application providers have the same reputation, features or level of integration as the Parties' software products. Although existing laptop application providers would offer some constraint on the merged entity post-acquisition, we are not satisfied that they will exert sufficient constraint on the merged entity to replace the lost competition between ATC and Serato with the Proposed Acquisition.

149.1. VirtualDJ, which would likely be the merged entity's largest competitor post-acquisition, was viewed by some as matching Serato on features, but was more commonly viewed as software that is primarily for beginner DJs.²¹³ One market participant described VirtualDJ as having the "stigma" of being consumer level software.²¹⁴ [

].²¹⁵ None of the DJs we spoke with mentioned VirtualDJ as an alternative if they were to switch to a different software brand.

²¹⁰ Serato "Submission in response to Commerce Commission Statement of Issues" (8 April 2024) at [103].

²¹¹ Commerce Commission meeting with Serato and ATC (29 April 2024).

²¹² Serato "Submission in response to Commerce Commission Statement of Issues" (8 April 2024) at [108].

²¹³ Commerce Commission interviews with [], [], [] and []. []

²¹⁴ Commerce Commission interview with [].

²¹⁵ Commerce Commission interview with [].

- 149.2. We do not consider that we can place much weight on Native Instrument’s Traktor software being a sufficient constraint on the merged entity. Market participants told us that while Traktor was once popular, it has now fallen behind the competition.²¹⁶ [] told us Traktor had lost market share by making “a lot of wrong decisions”.²¹⁷ [] software has “lost contact” with the features of competitors (for example, it currently lacks real time stem separation).²¹⁸
- 149.3. inMusic’s Engine DJ laptop application software is less feature-rich than the Parties’ software products as it is currently only able to be used for library management in preparation for a performance (meaning DJs are not able to use it as performance software). Engine DJ’s embedded software lacks the broader compatibility of other DJ software products as it is only able to be used with inMusic’s hardware products.²¹⁹ As such, both Engine DJ’s laptop application and embedded software offerings are unlikely to be seen by a sufficient number of DJs as a viable option for it to act as a constraint post-Acquisition.
- 149.4. Algoriddim’s djay software is considered more entry-level focused than the Parties’ software products.²²⁰ This is despite Algoriddim having a widely regarded real time stem separation functionality. [] told us that products that are integrated with djay are aimed at beginners/consumers whereas products that are integrated with Serato are aimed at professionals.²²¹ Some market participants also viewed Algoriddim as being more focused on Apple products such as iOS.²²² This means it may not be a good substitute for Serato customers who use laptops running Windows.
- 149.5. [] told us that it finds it difficult to compete with Serato and rekordbox when DJ hardware products and/or specific features of those products are locked to either of those laptop applications.²²³ [] noted that it is difficult to compete for professional DJ customers, for whom the integration of DJ software and DJ hardware is essential.²²⁴

²¹⁶ Commerce Commission interviews with [], [], [] and [].

²¹⁷ Commerce Commission interview with [].

²¹⁸ Commerce Commission interview with [].

²¹⁹ For completeness, we also consider that DJ hardware provider Hercules’ embedded DJ software product DJUCED is also likely to provide minimal competitive constraint post-acquisition for the same reason.

²²⁰ Commerce Commission interviews with [], [] and [].

²²¹ Commerce Commission interview with [].

²²² For example, [] said that aside from having a consumer focus, Algoriddim had an iOS focus. This was a market Serato did not reach, [] (Commerce Commission interview with []). [] told us it thought Algoriddim was attracting customers who were first time DJs and have decided to DJ on a tablet (Commerce Commission interview with []).

²²³ [].

²²⁴ [].

149.6. An internal document from Serato noted that [

].²²⁵

150. Figure 22 shows the MAU of DJ software products of the Parties and []. If the data showed that the increase in usage of [] was at the expense of Serato or rekordbox, then this would have been consistent with those DJ software products imposing a constraint. The chart does not show this. The chart does not include [].
151. The Parties' DJ software products are the most common software integrated with DJ hardware products (although for rekordbox this is due to it being integrated with ATC's Pioneer DJ hardware, which is the most popular brand of DJ hardware).
152. Integration with DJ software is important for DJ hardware competitors' ability to compete as integration makes a hardware product more desirable to consumers.
- 152.1. Software that is integrated with a piece of hardware works straight out of the box, without customers being required to make the software and hardware work (for example, through MIDI mapping, which we discuss further at paragraph [225]).
- 152.2. [] told us that having hardware integrate with Serato is important, that if the hardware doesn't integrate with Serato, he would think twice about using it. [] also told us that integrated gear keeps things simple, and that going forward he would only look at hardware if it integrates with Serato.²²⁶
- 152.3. [] told us that if he was to switch to a new DJ software provider, he would also switch DJ hardware providers as he would want the hardware he uses with the software to work "right away" rather than having to "do some tweaks" to make the hardware and software compatible.²²⁷
- 152.4. [] suggested that it is easier for consumers to buy hardware that already has the software integrated, rather than have to work to make the hardware and software compatible.²²⁸ It said that it might see the odd person MIDI mapping, but that it is not straightforward to do.
- 152.5. [] told us that people prefer to use the software that a hardware product was designed for.²²⁹ [] also said that it would not launch a hardware product without software integration, as it wants its products to work straight out of the box.²³⁰

²²⁵ [].

²²⁶ Commerce Commission interview with [].

²²⁷ Commerce Commission interview with [].

²²⁸ Commerce Commission interview with [].

²²⁹ Commerce Commission interview with [].

²³⁰ Commerce Commission interview with [].

- 152.6. [] told us that it benefits both software and hardware manufacturers to have extended compatibility.²³¹
- 152.7. [] noted that certain software performance features such as low-latency scratching can only be achieved through seamless hardware/software integration.²³² [] also noted that the bundling of software with hardware is a strong indication to consumers which DJ software to use with the hardware device they just purchased.²³³
153. DJ hardware providers told us Serato is the most important software to integrate their products with.²³⁴
- 153.1. [] told us Serato is the [] none of the other software alternatives have the same quality and adoption rate.²³⁵
- 153.2. [] told us that an estimated [] of its users use its hardware with Serato – as such, Serato integration is important due to its level of popularity.²³⁶ [] also noted the added value that including Serato in its products brings.²³⁷ [] told us that products with Serato sell better, that the strong sales are worth the long and expensive integration process and that it would not want to release a product without Serato integration.²³⁸ [] also said that without access to Serato, it could not meet the requirements of the professional DJs and advanced consumers DJs.²³⁹
- 153.3. [] told us that there are no other software companies it would partner with, and that every product has to have Serato integration to have saleability.²⁴⁰
154. Further to the above, DJ hardware providers did not indicate that partnering with a different DJ software provider was an option if Serato was unavailable. We consider that this strongly suggests that the other DJ software providers are not close competitors to Serato and are therefore unlikely to competitively constrain it.
155. We disagree with Serato’s argument that []

²³¹ Commerce Commission interview with [].

²³² [].

²³³ [].

²³⁴ []

[] also highlighted the importance of Serato, noting that customers will ask for a Serato controller, not a Pioneer DJ or Roland controller (Commerce Commission interview with []).

²³⁵ [].

²³⁶ Commerce Commission interview with [].

²³⁷ Commerce Commission interview with [].

²³⁸ Commerce Commission interview with [].

²³⁹ Commerce Commission interview with [].

²⁴⁰ Commerce Commission interview with [].

].

156. We also disagree with NERA’s submission that, post-acquisition, rivals could replace the lost competition between the Parties by repositioning their products to compete more closely with the products of the merged entity. The evidence we have viewed is that it is not that easy to reposition. For example, VirtualDJ [] and mobile apps would need to overcome being seen as for beginners. As we discuss further below at paragraphs [186]-[188], a DJ software provider is likely to face significant sunk costs in marketing to convince DJs that its product is a good alternative to those of the merged entity's.

Conclusion on constraint from competitors

157. In our view, the remaining DJ software competitors in the market are unlikely to provide sufficient constraint on the merged entity post-acquisition. The profitability of any price increase or quality decrease in the merged entity’s DJ software products is therefore unlikely to be defeated by these competitors responding or repositioning their products in the market. This would have the effect of substantially lessening competition in the DJ software market.

Out of market constraints – mobile app providers

ATC’s views

158. ATC submitted that mobile apps are a credible alternative and are rapidly gaining market share and providing an increasingly strong competitive constraint on DJ software.²⁴¹ According to ATC, mobile apps will become the preferred software for all types of DJing within the next five years.²⁴²
159. ATC submitted that laptop application and mobile app producer Algoriddim is one of the market participants that is well placed to continue to innovate and expand over the next five years.²⁴³ ATC also submitted that []²⁴⁴
160. In support of its argument that mobile apps are a constraint on laptop applications, ATC provided information on the growth of its mobile app users. []

²⁴¹ The Application at [1.4(b)].

²⁴² The Application at [6.13].

²⁴³ ATC “Submission by AlphaTheta Corporation on the Statement of Issues” (8 April 2024) at [6.12].

²⁴⁴ ATC “Confidential submission on Confidential Sol” (9 April 2024) at [1].

]:²⁴⁵

[

]

161. ATC told us that it [

].²⁴⁶ [

].²⁴⁷

162. NERA submitted that mobile apps will continue to provide a competitive constraint on the merged entity because:²⁴⁸

162.1. there is little quality difference between laptop applications and mobile apps in terms of essential features;

162.2. the cost of a user switching between a mobile app and a laptop application (or vice versa) is likely to be minimal; and

162.3. mobile app-only developers could switch and offer a laptop application option.

Serato's views

163. Serato submitted that the constraint from mobile apps should not be understated and argued that as most developments in the DJ software industry (such as stems technology that isolates parts of a song) have been driven by mobile apps, the constraint they are providing is strong and increasing.²⁴⁹

²⁴⁵ ATC RFI response 6 June 2024 p. 6.

²⁴⁶ ATC RFI response 6 June 2024 p. 10.

²⁴⁷ ATC RFI response 6 June 2024 p. 6.

²⁴⁸ NERA Economic Consulting "AlphaTheta Corporation/Serato: unilateral effects and foreclosure theories of harm" (27 November 2023) at [2.3].

²⁴⁹ Serato "Submission in response to Commerce Commission Statement of Issues" (8 April 2024) at [104].

164. Serato considers that mobile apps are used by all types of DJs, are capable of running all of the major features and special functions of most DJ hardware and that the small screen size of a phone or tablet is not an impediment, as the DJ is interacting with the DJ hardware, not the laptop, phone or tablet.²⁵⁰
165. Serato submitted that []²⁵¹ Serato also submitted that []²⁵²

Our assessment

166. As we set out in the market definition section at paragraphs [61]-[81], we are not satisfied that, post-acquisition, mobile apps are likely to be a viable alternative option for sufficient numbers of laptop application users. We have therefore assessed mobile apps as an out of market constraint. On balance, for the following reasons we do not consider that mobile apps would be able to exert meaningful competitive constraint on the merged entity.
167. The factors we set out earlier (at paragraphs [63]-[64]) that have influenced our views on why we do not agree with the Parties that laptop applications and mobile apps provide similar functionality (or are sufficiently substitutable products that they belong in the same market) are also relevant to our views on the level of competitive constraint that mobile apps impose upon laptop applications. In summary, we consider that most users of laptop applications will consider mobile apps an inferior product that they would be unwilling to switch to due to mobile apps' more limited features and more limited compatibility with DJ hardware compared to laptop applications.
168. The evidence collected during our investigation suggests that mobile apps are likely to predominantly be an option for beginner/learner DJs rather than all DJs (see paragraphs [69]-[75] above) and as such, will only provide limited constraint that is not felt across the entire market. This is based on:
- 168.1. Feedback from market participants, most of which told us that mobile apps are for beginners. For example:
- 168.1.1. [] told us that mobile apps are good for entry level customers.²⁵³

²⁵⁰ Serato "Submission in response to Commerce Commission Statement of Issues" (8 April 2024) at [15]-[29].

²⁵¹ Commerce Commission meeting with Serato and ATC (29 April 2024).

²⁵² Commerce Commission meeting with Serato and ATC (29 April 2024).

²⁵³ Commerce Commission interview with [].

168.1.2. [] told us that the less professional a DJ is, the more likely they are to use a mobile app.²⁵⁴

168.1.3. [] said it views mobile apps as a training ground, and introduction to the market.²⁵⁵

168.1.4. [] told us it sees mobile apps used more by beginner DJs rather than professionals. It also said it was not sure whether mobile app usage is growing among DJs.²⁵⁶

168.2. Internal documents from ATC indicate it views mobile apps as [].

168.2.1. [

].²⁵⁷

168.2.2. [

].²⁵⁸

169. We are not satisfied the evidence shows that laptop application providers consider mobile apps to be a threat (see paragraphs [76]-[80] above). We have not seen evidence that the rise in mobile apps usage has impacted on the growth rates of laptop application suppliers or led them to launch mobile apps. We do not agree with ATC that the graph it provided (at Figure 1, above) shows that the growth of its mobile app has been at the expense of its laptop application. While the chart shows rekordbox mobile app users are [

] it may be that mobile apps may be growing the market, capturing consumers that would otherwise not use any software at all. As such we are not satisfied that the rise in mobile app users has influenced the growth of laptop application users.

170. We agree with ATC that Algoriddim has contributed to innovation within the DJ software space and is well placed to continue to innovate. Despite this, we do not consider that Algoriddim is likely to provide sufficient constraint on the merged entity. This is because, like other mobile apps, Algoriddim is primarily viewed as

²⁵⁴ Commerce Commission interview with [].

²⁵⁵ Commerce Commission interview with [].

²⁵⁶ Commerce Commission interview with [].

²⁵⁷ [].

²⁵⁸ [].

software for beginner DJs. [

].²⁵⁹

Out of market constraints – music production software

ATC's views

171. ATC submitted that DJs can use Ableton Live, music production software that has DJ capabilities, to DJ. ATC submitted that Ableton is a substantial player in the music production industry, and is well placed to look to grow its share of the DJ software market²⁶⁰ and to continue to innovate and expand over the next five years.²⁶¹

Serato's views

172. Serato submitted that music production software will continue to act as a constraint as it is a viable option for a competitively significant portion of DJs.²⁶²

Our assessment

173. Feedback from market participants indicated that music production software is not likely to compete closely with DJ software as:

173.1. Music production software such as Ableton does not appear to be widely used for DJing:

173.1.1. one DJ hardware provider told us that while it would be possible to use music production software like Ableton to DJ, no one does it;²⁶³

173.1.2. one DJ software provider told us that no one purchases Ableton to DJ;²⁶⁴ and

173.1.3. another DJ software provider told us that while there are always exceptions, most DJs would not DJ with Ableton.²⁶⁵

173.2. Music production software has a different usage to DJ software and is a different market:

173.2.1. one software provider told us that there are some DJs using music production software as DJ software, but it is a very small chunk of

²⁵⁹ [].

²⁶⁰ The Application, at [6.24].

²⁶¹ ATC "Submission by AlphaTheta Corporation on the Statement of Issues" (8 April 2024) at [6.12(f)].

²⁶² Serato "Submission in response to Commerce Commission Statement of Issues" (8 April 2024) at [112].

²⁶³ Commerce Commission interview with [].

²⁶⁴ Commerce Commission interview with [].

²⁶⁵ Commerce Commission interview with [].

the market, and for people that are producers first and DJs second;²⁶⁶ and

- 173.2.2. another DJ software provider told us that you mix music with DJ software when you are performing live and use music production in the studio while you are trying to make a track.²⁶⁷
174. We consider that it is unlikely that a new DJ would choose music production software for DJing. The evidence we received during our investigation also did not suggest that if a DJ was to switch from using their existing laptop application, they would switch to using music production software ahead of switching to another laptop application. Music production software would only be a constraint in circumstances where the software includes the functionality needed to DJ and if the user is already familiar with the software.
175. We therefore consider that music production software would be likely to provide little to no constraint on the merged entity.

Conclusion on out of market constraints

176. In our view, out of market constraints such as mobile apps and music production software are unlikely to provide sufficient constraint on the merged entity post-acquisition. The profitability of any price increase or quality decrease in the merged entity's DJ software products is therefore unlikely to be defeated by consumers switching to mobile apps or music production software because these products are unlikely to be substitutes for laptop applications. This would have the effect of substantially lessening competition in the DJ software market.

Entry and expansion

ATC's views

177. ATC submitted that barriers to entry and expansion are low, especially for existing DJ software providers, for the reasons below.²⁶⁸
- 177.1. The time to develop and improve DJ software is not a barrier to entry, but rather a cost that all market participants incur. ATC said it took [] to develop the performance element of rekordbox.
- 177.2. Sunk costs are not a barrier to entry, as existing software providers are also subject to these costs and face similar expenditure for attracting new users.
- 177.3. The marginal costs associated with DJ software are low, and it is a highly scalable product. DJ hardware providers are well placed to enter/expand in the DJ software market in response to a price rise or decrease in quality.

²⁶⁶ Commerce Commission interview with [].

²⁶⁷ Commerce Commission interview with [].

²⁶⁸ ATC "Submission by AlphaTheta Corporation on the Statement of Issues" (8 April 2024) at [6.13]-[6.26].

177.4. Although there can be difficulties with getting DJs to switch providers, DJs will switch if their existing provider does not replicate a new feature or in response to a price rise or quality decrease. Further, switching difficulties do not apply to new users who have not yet established loyalty to a software.

178. In terms of information on customers switching between different DJ software products, ATC submitted that:²⁶⁹

178.1. [

178.2.

178.3.

].

179. NERA submitted that at a general level, barriers to entry and expansion into the DJ software market are likely to be low due to:²⁷⁰

179.1. switching costs for end users being relatively low, and switching not generally requiring a user to switch away from their existing hardware;

179.2. the nature of the product meaning that brand/reputation, while being an important dynamic in the market, is unlikely to constitute an economic barrier to entry; and

179.3. the costs of developing laptop application software being relatively low, with NERA estimating between [] to port (translate from one system to another) existing mobile software and [] to develop from scratch.

²⁶⁹ ATC RFI response (6 June 2024) pp. 9-10.

²⁷⁰ NERA Economic Consulting “AlphaTheta Corporation/Serato: unilateral effects and foreclosure theories of harm” (27 November 2023) at [2.1].

Serato's views

180. Serato submitted that competitors are well placed to expand in a timely manner, and that an existing competitor does not need to offer something completely new in order to expand.²⁷¹
181. Serato also submitted that:
- 181.1. There is compelling evidence to suggest DJs will switch providers based on an increase in price or decrease in quality.²⁷² From Serato's perspective, switching is "practically seamless" as rival DJ software automatically reads Serato's library, and the only switching costs a customer would face are any additional costs associated with purchasing a higher priced software.²⁷³
- 181.2. There are effective strategies that can be used to overcome difficulties with switching, such as creating software with a similar look/feel to existing products.²⁷⁴
- 181.3. Its analysis of customer churn data, which shows the rate of customers no longer using any Serato product, is evidence of customers switching.²⁷⁵
- 181.4. ATC's expansion into DJ software is evidence that DJ hardware providers face low barriers to entry as they are readily able to expand by using their existing presence in the market.²⁷⁶
- 181.5. Only [] of its [] R&D spend for 2022 was spent on funding ongoing R&D for its DJ software product.²⁷⁷
182. Serato submitted that a report from Clearpoint demonstrated that a full replica of Serato's DJ software, plus a mobile app, could be developed from scratch within a two-year period.²⁷⁸

²⁷¹ Serato "Submission in response to Commerce Commission Statement of Issues" (8 April 2024) at [116].

²⁷² In support of this, Serato cites some examples of high-profile switches from DJs such as DJ Angelo switching from Serato to djay and DJ Craze switching from Traktor to Serato. Serato "Submission in response to Commerce Commission Statement of Issues" (9 April 2024), at [122]- [130].

²⁷³ Serato "Submission on Statement of Unresolved Issues" (17 June 2024) at [36].

²⁷⁴ Serato "Submission in response to Commerce Commission Statement of Issues" (8 April 2024) at [119].

²⁷⁵ Serato "Submission in response to Commerce Commission Statement of Issues" (8 April 2024) at [128]- [130].

²⁷⁶ Serato "Submission in response to Commerce Commission Statement of Issues" (8 April 2024) at [118].

²⁷⁷ Serato "Submission in response to Commerce Commission Statement of Issues" (8 April 2024) at [115].

²⁷⁸ Serato "Submission in response to Commerce Commission Statement of Issues" (8 April 2024) at Appendix E.

183. The Clearpoint report provided a high-level estimate of the software engineering effort that would be required to build a competitive product to software such as Serato and VirtualDJ. Clearpoint concluded that:²⁷⁹
- 183.1. There did not appear to be any unique or novel constraints on a competitor building a software product to compete with Serato.
- 183.2. A new entrant could launch a product based on access to existing open-source components within 18 months, and an adjacent competitor (such as a music streaming service like Spotify) could launch a product based on its existing product/platform within 12 months.
- 183.3. The estimated cost of entry would be NZD\$7-9million, plus sales team and executive leadership salaries.
- 183.4. A new entrant would face some advantages, such as not having legacy code that would require updating, and a reduced product R&D cycle due to the ability to leverage product design from existing products.

Our assessment

184. We assess whether entry by new competitors or expansion by existing competitors is likely to be sufficient in extent in a timely fashion to constrain the merged firm and prevent a substantial lessening of competition. This is referred to as the ‘LET test’.
185. We are not satisfied that entry by new DJ software providers or expansion by existing DJ software providers would be sufficient to mean that the Proposed Acquisition is unlikely to give rise to a substantial lessening of competition in the supply of DJ software.
186. There are significant barriers to entry and expansion, including high fixed and sunk costs of developing software and high sunk costs of convincing customers to switch software providers. We also consider that the Proposed Acquisition is likely to raise strategic barriers to entry by enabling the merged entity to engage in conduct that makes it harder for competitors to enter and expand. However, even if these barriers can be overcome, the evidence indicates that entry or expansion that is sufficient to constrain the Parties would not occur in the time-frame relevant to our assessment. That is, we do not consider the LET test is satisfied.
187. As a starting point, we do not consider that there are clear examples of recent entry in the laptop application market. There does not appear to have been a major new entrant to the DJ software market since rekordbox (which first launched in 2009 as preparation software and then in 2015 with performance software). Participants in the DJ software market are all relatively mature (for example, VirtualDJ and Traktor entered the market in 2003 and 2000 respectively). While the lack of entry may reflect that there are no opportunities in the market (because existing players are

²⁷⁹ Serato “Submission in response to Commerce Commission Statement of Issues” (8 April 2024) at Appendix E.

already serving customers well), we consider that it is also likely to indicate that entry is more difficult than the Parties argued.

188. The evidence we received over the course of our investigation demonstrates that there are significant fixed and sunk costs in developing DJ software. The Clearpoint report estimated a build budget of NZD\$7-9million (excluding sales and executive leadership salaries). This figure appears small compared to the overall market size, which we estimate for CY2023 to be around []. Despite this (and assuming this figure is a reasonable estimate) this could still constitute a significant barrier to entry when other factors are taken into account.

188.1. First, the payback period is uncertain since it depends on what the number of subscribers and margins the entry could achieve. As a comparison we estimate that [

] has a global annual revenue from DJ software of around [].²⁸⁰

Given the following barriers to entry, it is unclear a new entrant would recover the build costs in a reasonable period of time. It may also be difficult for market participants that do not currently have a DJ software product to justify the cost of establishing one, particularly given the potential difficulties with securing sufficient scale (ie, sufficient customers switching from Serato or other software providers) to justify the investment. We discuss the stickiness of customers further below.

188.2. Second, the cost of entry and expansion may be largely sunk – once the investment in development has been made, it may not be possible to recover the costs except through successful trading. ATC submitted that the cost of developing DJ software is not a barrier to entry as it is a cost that all firms face. However, we consider it is relevant to consider any conditions that have the potential to hinder competition in the relevant market.²⁸¹ In this case, we consider the presence of sunk costs (costs that cannot be recouped upon exit) of developing software would constitute a barrier to entry because it increases the risk of entry. Failing to reach a sufficient scale means the investment may be lost. The difficulty to reach a scale to recoup the costs may potentially rise if ATC takes actions that inhibit the ability of DJ software providers to integrate with Pioneer DJ hardware, which we discuss further below.

²⁸⁰ [].

²⁸¹ This is consistent with the approach in *New Zealand Bus Ltd v Commerce Commission* [2007] NZCA 502 at [252] per Arnold J where he confirmed the approach of the High Court in *Commerce Commission v New Zealand Bus* and *Air New Zealand v Commerce Commission*. In those cases, the courts emphasised that the question of whether conditions in a market qualify as a barrier to entry, however defined, is less important than considering whether those conditions have the potential to prevent, impede or slow entry and expansion. *Commerce Commission v New Zealand Bus Ltd* (2006) 11 TCLR 679 (HC) at [147]-[155], citing Dennis Carlton “Why Barriers To Entry are Barriers to Understanding” (2004) 94 American Economics Review 466, and *Air New Zealand v Commerce Commission (No 6)* (2004) 11 TCLR 347 (HC) at [102].

189. The evidence we gathered over the course of our investigation also does not support the Parties' arguments that DJ software can be developed relatively quickly.

189.1. Estimates from market participants on the time to develop DJ software ranged from one to nine years, indicating that it can be a lengthy process.²⁸² We also understand that in some instances, software is developed over time and new iterations of software are built upon previous iterations.²⁸³

189.2. The timeframes set out in the Clearpoint report (that a new entrant or adjacent competitor could enter the market in 12-18 months) were within the lower bounds of the entry timeframes that market participants advised (which was one to nine years). However, we consider that the actual examples of entry timeframes from DJ software market participants are more probative than hypotheticals from non-market participants such as Clearpoint.

189.3. The timings set out in the Clearpoint report rely heavily on the new entrant being able to take advantage of existing open-source technology. While we understand that Algoriddim took advantage of open-source technology when developing its own versions of stems²⁸⁴ we are not satisfied that it would be a viable strategy to develop the bulk of a piece of software from open-source material, rather than simply using it to develop a standalone feature. There are likely to be risks associated with developing software that relies on a third party maintaining and supporting an element of that software in the absence of a formal contract.

189.4. Although it took ATC []²⁸⁵ to develop the performance element of rekordbox, we do not think that a new entrant could expect to develop performance software []. ATC already had somewhat of a head start having previously developed the library management side of the software – other market participants would not have this same advantage.

190. We understand that DJs are generally reluctant to change DJ software providers. DJing is a skill, and the live aspect of performing means there is little room for mistakes. Once a DJ is familiar with a piece of DJ software and knows that it works, they may be unwilling to try a new piece of software and risk something later going wrong when they are performing.²⁸⁶ We also understand that DJs tend to continue

²⁸² One software provider said it would “completely disagree” that DJ software could be built in under 12 months but said anyone could make software within three years (Commerce Commission interview with []). [] told us that it took eight-nine years to develop [] (Commerce Commission interview with []). [] told us that it took around a year to develop [] but that this was built on the previous version of the software (Commerce Commission interview with []).

²⁸³ Commerce Commission interviews with [], [] and [].

²⁸⁴ Serato “Submission in response to Commerce Commission Statement of Issues” (8 April 2024) at [105.4].

²⁸⁵ ATC “Submission by AlphaTheta Corporation on the Statement of Issues” (8 April 2024) at [6.19(a)].

²⁸⁶ Commerce Commission interview with [].

using what they started out DJing with, as it is easier to stick to what they are used to.²⁸⁷

191. We therefore consider that one of the most significant barriers to entry or expansion are these difficulties with convincing DJs to switch software providers and in securing new customers.

191.1. One DJ software provider told us there is a “huge inertia” in the DJ software market, and that DJs are reluctant to want to try new software.²⁸⁸ ATC itself [

].²⁸⁹ One DJ

hardware provider told us that while it could spend time making its own software, the market wouldn’t want it, as customers just want Serato.²⁹⁰ A retailer told us that DJs are more likely to change the DJ hardware they use than change DJ software providers.²⁹¹

191.2. This view was supported in most of our interviews with DJs. The majority of the DJs we spoke with were loyal to their existing DJ software provider (which in most instances was Serato).²⁹² This would make it even harder for a new DJ software brand to compete for existing Serato customers. While some of the evidence we gathered suggested that DJs may switch to a different software provider if their current one does not offer a particular new feature (such as stems),²⁹³ the overall stickiness of customers implies that switching costs are high, as customers appear to prefer to stick to the DJ software they know, rather than look for new alternatives.

191.3. The stickiness of DJs contributes to the risk of entry and adds to the sunk costs of advertising and promotion required to convince DJs to switch (these costs are sunk because, if the entry is unsuccessful, it is unlikely that these costs will be recoverable). The stickiness of customers to Serato is a key aspect of our vertical foreclosure concerns.

191.4. Although Serato has argued that its [

²⁸⁷ For example, one DJ told us that once you learn a bit of software, you don’t want to have to relearn another (Commerce Commission interview with [redacted]). Another told us that DJs will likely carry on using what they learnt to DJ on because it’s what they know (Commerce Commission interview with [redacted]). One software provider noted that DJs build muscle memory, and switching software would require learning new muscle memory (Commerce Commission interview with [redacted]).

²⁸⁸ Commerce Commission interview with [redacted].

²⁸⁹ ATC RFI response 6 June 2024 p. 10.

²⁹⁰ Commerce Commission interview with [redacted].

²⁹¹ Commerce Commission interview with [redacted].

²⁹² For example, one DJ told us there is nothing that would make him switch from Serato to another DJ software (Commerce Commission interview with [redacted]), another told us he has tried other software but always comes back to Serato (Commerce Commission interview with [redacted]).

²⁹³ Commerce Commission interviews with [redacted] and [redacted].

].

191.5. Our interviews with DJs did not support ATC's argument that []. []

].²⁹⁴ [].

191.6. While the Parties argued that customers can and do switch, they did not provide compelling evidence in support of this argument (and in fact ATC []).

192. ATC submitted that []. As we explain in paragraph [75], to the extent competition takes place between mobile apps and laptop applications to capture new users it does not imply mobile apps will impose a strong constraint on laptop applications. As we explain in the market definition section, mobile apps may not be a good substitute for DJs that are currently using laptop applications or once the DJ has progressed beyond beginner level.
193. While the rise in the use of cloud-based music streaming services may reduce barriers to consumers switching, this will be of most use only for DJs that have not already prepared music libraries in their DJ software of choice. We understand that over the course of a DJ's career they build up their music library, adding cues and loops and preparing playlists, and that this information often cannot be easily transferred across to a new piece of software. For example, [] told us there is no officially supported software that will facilitate this²⁹⁵ and [] told us that it is difficult or impossible for rekordbox customers to switch to its DJ software because users cannot migrate their playlists and metadata created in rekordbox over to its software.²⁹⁶ Post-acquisition, ATC would be in a position to raise switching costs by making it difficult to move track information from rekordbox or Serato to another DJ software provider.
194. We are also of the view that, even if a new entrant was able to overcome these barriers and enter the market, mere entry alone is unlikely to be sufficient to act as a constraint on the merged entity. The entrant would likely need to offer something new in order to be considered as a viable option, and DJs would need to see the new software as a genuine alternative in order for the software to provide any

²⁹⁴ Commerce Commission interview with []. Another DJ said that neither he nor any of the DJs at his company use different kinds of software. He likened it to a person's phone, and noted that people don't switch between Apple and Android all the time (Commerce Commission interview with []).

²⁹⁵ Commerce Commission interview with [].

²⁹⁶ [].

meaningful constraint.²⁹⁷ This means there is likely to be a delay between entry and the time when the software has reached sufficient scale to impose a strong competitive constraint in the market.²⁹⁸ We consider this is unlikely to occur within one to two years.

195. We note that existing DJ hardware providers such as inMusic and Hercules have both entered the DJ software space and developed DJ software for use with their respective DJ hardware brands. However, we consider that these examples are strong evidence that mere entry to the market does not automatically equate to the entrant being a significant enough competitor.

195.1. inMusic and Hercules' DJ software products are at this stage only compatible with the DJ hardware providers' respective products and cannot be used with some of the hardware that Serato users own. They also do not appear to be particularly well-regarded among market participants.²⁹⁹ As a result, their entry into the DJ software market does not appear to have sufficiently constrained Serato and rekordbox, and would be unlikely to constrain the merged entity in the future.

195.2. We do not see any reason why another DJ hardware provider's entry into the DJ software market would be more successful than the above providers. While ATC is a DJ hardware provider that has had success in quickly growing its market share in the DJ software space, it did so off the back of a very strong presence and reputation in the DJ hardware market. Being able to leverage its existing large user base inevitably gave ATC an advantage in growing its user base for DJ software (and is another reason why we consider that ATC may impose a strong competitive threat to Serato). Other DJ hardware providers do not have ATC's presence in the DJ hardware market, so would not have the same ability to do this. We therefore do not accept that ATC's success in DJ software is indicative of the success other DJ hardware providers could expect should they enter the DJ software market.

195.3. DJ hardware providers other than ATC would likely require significant investment of the nature described earlier to make their products attractive to Serato users and to develop the product to the point at which it would act as a constraint. However, without the users to guarantee this, spending the money required to develop the software might not be a desirable prospect.

196. Lastly, ATC could materially influence barriers to entry and expansion through inhibiting interoperability with its devices. ATC supplies around [] of the DJ hardware market.³⁰⁰ The inability for a DJ software competitor to interoperate with

²⁹⁷ For example, [] told us that a new entrant would need to offer something new to the market – merely replicating Serato wouldn't be enough to win customers (Commerce Commission interview with []).

²⁹⁸ The Clearpoint report did not address this.

²⁹⁹ For example, one market participant noted that DJUCED is technically behind compared to other DJ software providers (Commerce Commission interview with []).

³⁰⁰ See AlphaTheta/Serato Statement of Issues at Table 3.

the hardware that accounts for [] of the market may materially influence their decision to invest in entry or expansion. It would be particularly hard for any competitor to sufficiently replace the lost competition between rekordbox (which is used with ATC’s devices) and Serato if the rival DJ software does not work with ATC’s devices. We understand this may already be happening to a degree.

196.1. [

].³⁰¹ [

].³⁰²

196.2. One of [] concerns with the Proposed Acquisition is ATC preventing [] software from being compatible with Pioneer DJ hardware. [] told us that this would have a “massive impact” and be the “worst case” scenario.³⁰³ It also told us that it has had experience with being [

].³⁰⁴

196.3. [] said that it is “very afraid” that ATC would close off its access to Pioneer DJ hardware.³⁰⁵ As an estimated [] of [] users use the software with Pioneer DJ hardware, being cut-off from that hardware would cause it to lose a lot of its customers.³⁰⁶ [] said that ATC locking out all DJ software competitors would effectively “kill” the competitors and any future innovation.³⁰⁷ Such conduct would prevent developers being incentivised to create DJ software because most DJs appear to want to buy Pioneer DJ hardware.³⁰⁸

197. We do however accept Clearpoint’s argument that a new entrant would have some advantages over incumbents, such as not having legacy code that requires updating. For example, []³⁰⁹ However, we have not received compelling evidence of any other advantages a new entrant would have and are not satisfied this would be sufficient to overcome other barriers in the market.

³⁰¹ [].

³⁰² [].

³⁰³ Commerce Commission interview with [].

³⁰⁴ Commerce Commission interview with [].

³⁰⁵ Commerce Commission interview with [].

³⁰⁶ Commerce Commission interview with [].

³⁰⁷ Commerce Commission interview with [].

³⁰⁸ Commerce Commission interview with [].

³⁰⁹ Commerce Commission interview with [].

Conclusion on unilateral effects

198. We are not satisfied that the Proposed Acquisition would not have, or would not be likely to have, the effect of substantially lessening competition in the DJ software market due to unilateral effects.
199. In weighing up all of the evidence, we are not satisfied that any of the remaining constraints would be sufficient to constrain the merged entity post-acquisition. We are also not satisfied that the combination of the remaining constraints would be sufficient to constrain the merged entity post-acquisition. That is, we do not consider that the collective constraint from existing DJ software providers, constraint from DJ software providers that sit outside the market (such as mobile apps, music production software and embedded software) as well as the potential for entry and expansion, would be strong enough to prevent the merged entity from increasing the price or decreasing the quality of its software offerings post-acquisition relative to counterfactual.

Competition analysis – vertical effects

200. A substantial lessening of competition can arise when one party acquires another party that is not a competitor in the same market, but is a participant in a related market. This can occur where the acquisition gives the acquiring firm a greater ability and/or incentive to engage in conduct that prevents or hinders competitors from competing effectively in either market.³¹⁰ The means through which a firm could achieve this include:
- 200.1. refusing to deal with competitors completely (total foreclosure); or
- 200.2. raising the price it charges these competitors (partial foreclosure).
201. A substantial lessening of competition may arise where foreclosure makes entry and expansion more difficult, or otherwise reduces a competitor's (or competitors') ability to provide a competitive constraint. Foreclosure does not need to force a competitor, or competitors, to exit the market to have this effect.³¹¹
202. We are not satisfied that the Proposed Acquisition will not have, or would not be likely to have, the effect of substantially lessening competition in the DJ hardware market as a result of vertical effects. As we explain below, the main reasons are:
- 202.1. the merged entity would be likely to have the market power for DJ software to foreclose DJ hardware rivals and likely to have a mechanism to raise the costs of rivals';
- 202.2. we are not satisfied the merged entity would not have an incentive to foreclose DJ hardware competitors; and

³¹⁰ Mergers and Acquisitions Guidelines above n3 at [5.1]-[5.2].

³¹¹ Mergers and Acquisitions Guidelines above n3 at [5.10].

202.3. such foreclosure is likely to adversely affect competition for the supply of DJ hardware.

Ability to foreclose DJ hardware competitors

203. A firm may have the ability to foreclose competitors where it has market power at one or more levels of the supply chain, and so controls a significant proportion of an input or customer base.³¹² If a firm does not have market power, then its competitors could switch to alternative suppliers (or buyers) to defeat the firm's foreclosure strategy. We considered whether ATC would have the ability to foreclose competitors in the DJ hardware market post-acquisition.
204. We consider that the merged entity would likely have market power for the supply of DJ software with the acquisition. We consider that it would likely have a range of options available to it to foreclose competitors in the DJ hardware market (and potentially also the DJ software market, which we discuss separately) such as raising the cost of the fee to license Serato, refusing to allow DJ hardware providers to integrate with Serato, delaying integration or integrating less completely, or tying or bundling products. We do not think that the SPA would be sufficient to protect competitors in the DJ hardware market.

ATC's views

205. ATC submitted that the merged entity would not have the ability to foreclose competitors for the reasons set out below.
- 205.1. Users can integrate their hardware with Serato by 'MIDI mapping' (where a DJ manually assigns buttons, faders and knobs on their hardware to control features in the software). ATC submitted that MIDI mapping does not require an arrangement between the DJ hardware provider and Serato³¹³ and can be done as long as the device has a sound card supported by Serato (which ATC said the most popular software generally has).³¹⁴
- 205.2. The terms of the SPA preclude ATC refusing to allow Serato to partner with other DJ hardware brands or making Serato less attractive to partner with.³¹⁵
206. ATC submitted that, even absent the SPA provisions, it would have no ability to foreclose DJ hardware competitors. This is because:³¹⁶
- 206.1. Serato is not an essential input – it has a [] market share based on MAU, there are a large number of alternative DJ software options and DJ hardware competitors market their products with DJ software partners other than Serato (eg, in FY23 the top three best-selling DJ controllers were compatible with more than three laptop applications).

³¹² Mergers and Acquisitions Guidelines above n3 at [5.7].

³¹³ The Application at [7.6].

³¹⁴ The Application at [7.6].

³¹⁵ The Application at [7.20]-[7.24].

³¹⁶ ATC "Submission by AlphaTheta Corporation on the Statement of Issues" (8 April 2024) at [7.49]-[7.64].

- 206.2. The DJ software market is dynamic – it is highly unlikely Serato would become essential by the time the Contingent Consideration Period (the period ending 31 December 2028) ends given the strong growth of mobile apps and DJ hardware with embedded software.
- 206.3. There is no mechanism to foreclose – ATC could not prevent non-ATC hardware users from using existing versions of Serato and it is possible to MIDI map Serato software to DJ hardware.
207. ATC submitted that the terms of the SPA preclude foreclosure during the Contingent Consideration Period.³¹⁷
- 207.1. The SPA contains [] contingent payments based on []].
- 207.2. The SPA contains protections for the sellers of Serato (the Sellers) designed to ensure the buyer does not interfere with the Serato business so as to detrimentally affect the earnout potentially payable to the Sellers. ATC submitted that such protections would prevent foreclosure by the merged entity because if ATC breached those protections it would have to pay Serato and that Serato employees (who stand to gain from the earnout) will be motivated to enforce the protections. The protections include that:³¹⁸
- 207.2.1. [ATC] undertakes to the Sellers that it will, during the Contingent Consideration Period, act in good faith and, using all reasonable endeavours, support the growth of and operate and manage [Serato] with a view of maximising the [relevant profit metric]” (clause 6.1, Schedule 11);
- 207.2.2. “[ATC] will ensure that [Serato] is managed in a prudent manner consistent with the 12 months immediately prior to Completion” (clause 6.2.1, Schedule 11); and
- 207.2.3. “[ATC] will ensure that [Serato] does not (without the prior written consent of the Sellers’ Representative)...materially change the nature or scope of its Business as presently conducted...” (clause 6.2.9(a), Schedule 11).

³¹⁷ ATC “Submission by AlphaTheta Corporation on the Statement of Issues” (8 April 2024) at [7.7]-[7.35].

³¹⁸ ATC “Submission by AlphaTheta Corporation on the Statement of Issues” (8 April 2024) at [7.19].

208. ATC submitted that there is no credible likelihood of vertical foreclosure in the DJ hardware market, and that for a foreclosure theory of harm to be made out the Commission would need to conclude:³¹⁹

208.1. there is a real and substantial risk that during the period until the end of the Contingent Consideration Period, ATC would engage in conduct in breach of its obligations under the SPA; and

208.2. that absent the SPA conditions there is a real and substantial risk that ATC would have the ability and incentive to foreclose competitors, and that this would have the effect of causing an SLC.

209. ATC also submitted that [

].³²⁰

Serato's views

210. Serato also submitted that the Proposed Acquisition will not substantially lessen competition in the DJ hardware market due to vertical effects.

211. Serato said it does not have the ability to foreclose competitors as it is not a “must have” product.³²¹ Serato argued that this means that any attempt by ATC to foreclose competitors would be ineffective and counterproductive. In support of this, Serato noted that:

211.1. software products other than Serato are commonly used and endorsed by high-profile DJs;³²²

211.2. Serato is [], as it does not have an iOS or Android app and has been unable to secure music streaming integration for its software from major music streaming platforms such as Spotify, Apple or Amazon;³²³

211.3. [],³²⁴

211.4. many companies have successfully released new hardware with no Serato association;³²⁵

³¹⁹ ATC “Submission by AlphaTheta Corporation on the Statement of Issues” (8 April 2024) at [7.5].

³²⁰ Email from ATC with comments on unredacted SoUI (20 June 2024).

³²¹ Serato “Submission on Statement of Preliminary Issues” (9 November 2023) at [4]-[6].

³²² Serato “Submission on Statement of Preliminary Issues” (9 November 2023) at [6].

³²³ Serato “Submission on Statement of Preliminary Issues” (9 November 2023) at [7].

³²⁴ Serato “Submission on Statement of Preliminary Issues” (9 November 2023) at [10].

³²⁵ Serato “Submission on Statement of Preliminary Issues” (9 November 2023) at [16].

211.5. DJ hardware providers' ability to create embedded software options has reduced their reliance on third party software providers,³²⁶

211.6. [

];³²⁷ and

211.7. Serato is not "must have" now and will be even less likely to be one after the Contingent Consideration Period ends.³²⁸

211.7.1. The proportion of DJ hardware products that are marketed with Serato as the primary software has declined rapidly. In FY18, Serato was the primary software for 100% of DJ controllers released whereas in FY24 this percentage dropped to [].

211.7.2. In FY24 only [] of new hardware supported by Serato bears Serato branding.

211.7.3. DJ hardware competitors have been launching products without official support from Serato (with Serato support coming later) or have launched products with no Serato support.

212. Serato submitted that the protections in the SPA would prevent foreclosure because.³²⁹

212.1. The foreclosure conduct would be a breach of the SPA obligations.

212.2. The Sellers and key employees are beneficiaries of the earnout, so would be greatly motivated to ensure ATC adheres to the seller protections.

212.3. The seller protections are robust and enforceable, and not "watered-down" protections that are difficult to prove or enforce. While there are potential risks associated with litigation, ATC has much more to lose and is thus more likely to be wary of litigation risk due to the damage to ATC's reputation and goodwill.

212.4. Serato will not be less motivated to enforce the SPA at the end of the term because the earnout is based on [].

³²⁶ Serato "Submission on Statement of Preliminary Issues" (9 November 2023) at [17].

³²⁷ Serato "Submission on Statement of Preliminary Issues" (9 November 2023) at [19]-[20].

³²⁸ Serato "Submission in response to Commerce Commission Statement of Issues" (8 April 2024) at [142] and [186].

³²⁹ Serato "Submission in response to Commerce Commission Statement of Issues" (8 April 2024) at [143]-[151].

213. Serato also submitted that:³³⁰

213.1. Serato's path to market is via its DJ hardware partners, and that any damage to its relationship with these partners would harm its bottom line.

213.2. The SPA provisions exist to confirm that ATC would not be able to compromise Serato's relationships with these partners, thereby compromising the amount of the earnout the Sellers would receive.

213.3. There is no basis in law for the view that the SPA provisions must be able to be enforced by third parties. The SPA provisions form part of the factual and cannot be ignored.

214. Serato stated that [

].³³¹ Serato also asserted [

].³³²

215. Serato also submitted that its existing agreements with DJ hardware providers prevent it from foreclosing those competitors.³³³ These contracts require Serato to support the software products already supplied to its DJ hardware partners, and run until at least [] and longer for some parties.

Our assessment of the merged entity's ability to foreclose competitors

216. We are of the view that the merged entity would have the ability to foreclose its competitors in the DJ hardware market. This because with the Proposed Acquisition it would have market power for the supply of DJ software and would have a number of mechanisms through which it could implement a foreclosure strategy. We do not think that the SPA would be sufficient to protect competitors in the DJ hardware market.

The merged entity is likely to have market power for the supply of DJ software to DJ hardware providers

217. The evidence we gathered over the course of our investigation suggests that Serato has market power for the supply of DJ software to DJ hardware providers.

218. First, Serato is the most important DJ software for DJ hardware providers to integrate with. The evidence supports the Parties' claims that hardware is less

³³⁰ Serato "Submission on Statement of Unresolved Issues" (17 June 2024) at [23]-[25].

³³¹ Commerce Commission interview with Serato (27 November 2023).

³³² Commerce Commission interview with Serato (27 November 2023).

³³³ Serato "Submission in response to Commerce Commission Statement of Issues" (8 April 2024) at [157]-[160].

frequently being released with Serato as the only officially supported software, and [redacted]. Despite this, the evidence still shows that rival DJ hardware providers remain heavily reliant on integration with Serato.

218.1. Although hardware is now being released with support for multiple DJ software, the [redacted] of DJ hardware is still shipped with support for Serato. For example, we estimate based on CY22 data, around [redacted] of controller and all-in-one units shipped by [redacted] (who are some of ATC's major DJ hardware competitors) come with Serato pre-mapped. As noted in paragraph [153] [redacted] told us that Serato remains the most important software to integrate DJ hardware products with.

218.2. An ATC internal document states [redacted]

[redacted].³³⁴ Even though ATC has developed its own DJ software (rekordbox), ATC still pays royalties to integrate its products with Serato.

219. Second, we do not consider DJ hardware providers' ability to switch to integrating their products with other software providers is sufficient to constrain the merged entity's ability to pursue a foreclosure strategy. DJ hardware providers told us that they would not see any other DJ software providers as an option to bundle their hardware with if Serato was no longer available.^{335 336}

219.1. The most common alternative laptop applications that DJ hardware is integrated with (aside from Serato) are rekordbox and Algoriddim. However, we are not satisfied these are likely to be good alternatives for DJ hardware competitors.

219.1.1. If the merged entity was to engage in a foreclosure strategy, then it is unlikely to make rekordbox (which it owns) available to DJ hardware competitors. Even if it was made available, DJ hardware competitors are unlikely to see rekordbox as an option since it would expose them to similar risks they face with Serato. For example, they may be hindered from fully integrating and would need to pass over commercially sensitive information.

219.1.2. Adding integration with Algoriddim grows the opportunities for DJ hardware providers to make sales but does not replace the need to integrate with Serato. As noted earlier, Algoriddim appears to be targeted at a different group of customers (ie, beginners, or customers that own Apple products) and therefore is unlikely to be a good alternative for DJ hardware providers who wish to sell to

³³⁴ [redacted].

³³⁵ Commerce Commission interviews with [redacted], [redacted] and [redacted]. [redacted].

³³⁶ Embedded software is not a suitable alternative for this purpose. Embedded software is used to operate DJ hardware such as all-in-ones and CDJs. It can only be used on the DJ hardware in which it is embedded.

more professional DJs or non-Apple users. This evidence is consistent with the views of [] all of which view Serato as essential to the success of their products.³³⁷

219.2. We are not satisfied that VirtualDJ would be a suitable option for DJ hardware providers to integrate their hardware with if the merged entity pursued a foreclosure strategy. As we have noted previously, VirtualDJ's software is primarily seen as being for beginner DJs. It may therefore not have sufficient pull with customers, such that it would be a replacement to Serato for DJ hardware providers to partner with.

219.3. While the use of mobile apps is growing, we are not satisfied that DJ hardware providers could switch to integrating their products with mobile apps in order to defeat a foreclosure strategy. As we noted earlier, the evidence does not show that the growth of mobile apps is at the expense of laptop applications used with DJ hardware – they instead seem targeted at a different customer group.

219.4. Lastly, as we identified in paragraphs [184]-[194], we consider there are barriers to entry and expansion that would inhibit an alternative DJ software supplier emerging that DJ hardware providers could switch to integrating their products with in order to defeat a foreclosure strategy. We also consider that DJ hardware providers would face similar barriers in creating their own embedded software. Further, while inMusic has created its own embedded software it still has products that are integrated with Serato. This suggests that a hardware provider's ability to create embedded software is not sufficient to reduce that provider's reliance on third party software providers.

220. Serato's lack of a mobile app and lack of widespread streaming integration does not appear to have affected its market power.

220.1. Serato's MAU []³³⁸ and, as we note earlier, Serato has []³³⁹ [].

220.2. DJ software providers appear to be on a similar playing field in terms of the level of streaming integration. No software provider has music streaming

³³⁷ [] stated that Algoriddim was focused on iOS, iPhone and iPad and was for consumers whereas Serato was more for professionals (Mac and PC) (Commerce Commission interview with []).

[] (Commerce Commission interview with []). [] said dJ Pro (ie, Algoriddim) was likely the closest alternative to Serato but it was not the solution because the market would not accept it and it was not [] market (Commerce Commission interview with []).

³³⁸ See Figure 1.

³³⁹ [].

integration for Spotify, only inMusic has secured integration with Amazon and only Algoriddim has secured integration with Apple.

ATC would have mechanisms to foreclose competitors

221. There are a range of potential mechanisms which the merged entity could use to foreclose competitors in the DJ hardware market by raising their costs. For example, these could include, but are not limited to:
- 221.1. raising the cost of the software licence fee (and other engineering fees);
 - 221.2. refusing to integrate, delaying integration or integrating less completely (such as only allowing certain features to work with a controller);
 - 221.3. gaining access to sensitive information of competitors (including on unreleased products and user device data) (which we discuss separately below); and
 - 221.4. tying or bundling Serato with ATC's Pioneer DJ hardware products (for example, offering a Pioneer DJ and Serato bundle at a discount).
222. These foreclosure mechanisms do not involve outright refusal to engage with competitors (total foreclosure), rather they involve steps to, over time, make it incrementally more difficult for competitors to engage and compete in the DJ hardware market (partial foreclosure). These mechanisms would substantially lessen competition by making it more difficult for rival hardware competitors to compete, as they could not access Serato software, or not access it on terms that allow them to viably compete.

The SPA does not provide sufficient protections to constrain the ability to foreclose

223. We are not satisfied that the SPA provisions would constrain the merged entity's ability to foreclose competitors in the DJ hardware market. This is because:
- 223.1. Those provisions of the SPA confer private law rights which only the Sellers could enforce. Third party DJ hardware providers – who would be negatively affected by foreclosure – and the Commission would have no ability to do so.
 - 223.2. There are many reasons why the Sellers may not seek to enforce the SPA provisions if ATC sought to foreclose competitors in the DJ hardware market:
 - 223.2.1. Any steps ATC may take to foreclose DJ hardware competitors seeking to partner with Serato will not necessarily negatively impact the financial interests of the Sellers. As detailed below, there are scenarios where we consider it would be in the interests of the Sellers to exclude DJ hardware competitors.
 - 223.2.2. In such scenarios, there would be no incentive for the Sellers to enforce the relevant provisions. inMusic provides the example of

brand licensing “Serato” for Pioneer DJ hardware products.³⁴⁰

Provided this potential action remained in the financial interests of Sellers (ie, had a positive outcome), which it would, it is unlikely that any action would be taken to mitigate the competition impact of this action.

223.3. Even if the Sellers did seek to enforce a breach of the relevant provisions, the most likely remedy would be an award of damages to the Sellers to compensate it for the earnout entitlement that it would have received but for the breach. Although that remedy would compensate the Sellers for the financial effects of breach, it would not constrain the foreclosure conduct or the effect of it on competitors.

223.4. In addition, even if the Sellers were incentivised to enforce the protections, there are a range of mechanisms that ATC could use to foreclose DJ hardware competitors that would, at least arguably, not breach the SPA provisions. The more subtle the foreclosure, the more challenging it will be for the Sellers to prove that ATC is in breach of the relevant provisions, which is likely to lower the chances of the Sellers taking action under the relevant provisions. The provisions of the SPA are expressed in broad terms designed to protect the financial interests of the Sellers; they are not drafted to mitigate competition concerns.

223.5. There are a number of ways ATC could act against the interests of DJ hardware competitors, whilst still remaining in compliance with its broadly drafted obligations under the SPA. For example, it could:

223.5.1. impose commercial strategies that have the effect of constraining internal resourcing decisions, in terms of the time and cost for development and integration of different Serato products, which could ultimately result in the deprioritisation of these processes with certain hardware partners over time; or

223.5.2. encourage the development of different variations of Serato software to be offered to different DJ hardware providers, in order to complement the specific design or features of the relevant hardware. Over time, this may result in certain features which are developed with Pioneer DJ hardware being restricted to Pioneer DJ products.

223.6. As noted by Serato,³⁴¹ the SPA provisions are premised on the general requirement that ATC will “act in good faith” and, use “all reasonable endeavours” support the growth of Serato and maximise [].³⁴² Where the foreclosure is very subtle, demonstrating that ATC has

³⁴⁰ inMusic Cross Submission on the Statement of Issues (25 April 2024) at [48(c)].

³⁴¹ Serato “Submission in response to Commerce Commission Statement of Issues” (8 April 2024) at Appendix B, paragraph 8.

³⁴² [].

failed to meet the expectations established by these legal concepts will require the Sellers to engage in considerable factual analysis and legal argument regarding the nature of ATC's breach and the alternative options available to it at the time. This would be a resource intensive exercise.

223.6.1. Even if it could be established that ATC has imposed commercial strategies that ultimately mean, for example, ATC has not continued to offer Serato products to Serato's existing and prospective customers, provided ATC can show that it has nonetheless acted in good faith with a view to supporting the growth of Serato, it would be able to contest whether it has in fact breached the provisions established by the SPA.

223.6.2. The fact of this contestability, in and of itself, raises concerns about the constraining effect of the SPA provisions. It means that enforcing the protections would be uncertain and resource intensive for the Sellers. This would have bearing on whether they would seek to enforce them.

223.7. The contracting parties could waive or renegotiate the SPA provisions by mutual consent. [

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223.7.1. This means that the scope for the Sellers to enforce a breach of the protections is limited, as the SPA mandates [

].

223.7.2. Because Schedule 11 [

]. As noted above, that would not address the competition concerns arising from the ability to foreclose DJ hardware competitors.

224. Finally, even if the SPA provisions offer some protection against foreclosure conduct, they are temporary. Following the expiration of the provisions, ATC would be free to

take all of the actions that the SPA provisions might otherwise preclude. We discuss this further below at paragraphs [273]-[280].

MIDI mapping does not bypass the need for integration

225. The evidence we received over the course of our investigation is not persuasive that the ability to MIDI map is sufficient to constrain the merged entity's ability to foreclose DJ hardware competitors.

225.1. While MIDI mapping may be possible, we understand that customers are likely to have a stronger preference for DJ hardware and DJ software that is already integrated, without them needing to carry out extra work to do this. Some customers may be unable to MIDI map, or simply put off from purchasing those devices that would require this due to the inconvenience of MIDI mapping.

225.1.1. One DJ that we spoke with said that integration with Serato is important, and that they would think twice about using any gear that doesn't naturally integrate, or would be difficult to integrate, with Serato.³⁴³

225.1.2. [] suggested that it is easier for consumers to buy hardware that already has the software integrated, rather than have to work to make the hardware and software compatible.³⁴⁴ It said that it might see the occasional person MIDI mapping, but that it is not straightforward to do.

225.2. Some market participants told us that MIDI mapping is not likely to be a substitute for full integration as it does not allow for in depth integration of all of the functions and provides a lower quality outcome for the user.³⁴⁵

225.3. inMusic and [] both noted that Serato is particularly challenging to MIDI map, and that there are some features of Serato that customers cannot MIDI map (such as screens, which typically require a deeper level of integration through HID mapping).³⁴⁶

225.4. If MIDI mapping was a good alternative to integration, it is unclear why DJ hardware providers would put so much effort in working with Serato to integrate their products and then pay a fee to Serato for all the devices sold.

³⁴³ Commerce Commission interview with [].

³⁴⁴ Commerce Commission interview with [].

³⁴⁵ Commerce Commission interviews with [], [] and []. [].

³⁴⁶ inMusic "inMusic's Response to Serato Audio Research Limited's Submission in Support of AlphaTheta Corporation's Clearance Application to Acquire Serato" (22 November 2023) at [II.c] and Commerce Commission interview with [].

Existing agreements between Serato and hardware manufacturers do not confer protection

226. Serato argues that its existing [] will prevent it from foreclosing hardware manufacturers.³⁴⁷

227. []:

227.1. [];

];³⁴⁸

227.2. [];

];³⁴⁹ and

227.3. it is unclear how [] will preclude Serato from carrying out subtle foreclosure strategies by, for example, (as noted above):

227.3.1. raising the cost of the software licence fee over time (and other engineering fees); or

227.3.2. delaying integration or integrating new software features less completely (such as only allowing certain updated features to work with a particular controller).

Conclusion

228. We are not satisfied that the merged entity would not have the ability to foreclose competitors in the DJ hardware market. Post-acquisition, the merged entity would have control of Serato, which is an important input. We are not satisfied the SPA provisions, terms of existing software agreements, or the ability to MIDI map are likely to constrain the merged entity's ability to foreclose.

Incentive to foreclose DJ hardware competitors

229. The merged entity would only rationally foreclose competitors if it is profitable to do so. If the merged entity attempted to foreclose rivals by raising their costs (such as refusing or inhibiting the ability for DJ hardware providers to integrate with Serato), it would have the following effects:

³⁴⁷ Serato "Submission in response to Commerce Commission Statement of Issues" (8 April 2024) at [157]-[160].

³⁴⁸ [].

³⁴⁹ [].

- 229.1. the merged entity would lose profits from selling fewer Serato software licences to rival DJ hardware providers; but
- 229.2. the merged entity would gain profits from all those customers that switched from buying a controller from rival DJ hardware providers to purchasing an ATC controller.
230. As we explain below, we are not satisfied that ATC would not have the incentive to foreclose its DJ hardware competitors.

ATC's views

231. ATC submitted that it would have no incentive to refuse to partner with other DJ hardware brands and/or make Serato less attractive to rival DJ hardware brands.³⁵⁰
232. ATC submitted that it has no incentive to breach the SPA and to suggest otherwise would be 'pure speculation'.³⁵¹ ATC said it would be subject to monitoring and significant financial consequences,³⁵² and a breach of the SPA would cause significant damage to ATC's reputation.³⁵³
233. ATC submitted that there is no prospect of the SPA being renegotiated.³⁵⁴ ATC would not be willing to pay Serato's valuation of the business – this was the reason for the earnout. There is no reason why Serato would waive the SPA conditions as it would adversely affect the earnout.
234. ATC submitted that it has no incentive to foreclose because:³⁵⁵
- 234.1. Engaging in foreclosure would reduce the value of the Serato business and trigger an impairment risk for ATC's parent company.
- 234.2. ATC has no history of attempting to foreclose its competitors.
- 234.3. A foreclosure strategy is not consistent with ATC's strategy.³⁵⁶
- 234.4. Growing DJ software is just as important as ATC's hardware business.

³⁵⁰ The Application at [7.15]-[7.19].

³⁵¹ ATC "Submission by AlphaTheta Corporation on the Statement of Issues" (8 April 2024) at [7.37].

³⁵² [

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³⁵³ ATC "Submission by AlphaTheta Corporation on the Statement of Issues" (8 April 2024) at [7.39]-[7.44].

³⁵⁴ ATC "Submission by AlphaTheta Corporation on the Statement of Issues" (8 April 2024) at [7.32]-[7.35].

³⁵⁵ ATC "Submission by AlphaTheta Corporation on the Statement of Issues" (8 April 2024) at [8.1].

³⁵⁶ [

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- 234.5. Engaging in foreclosure would damage the Parties' reputations (resulting in an immediate loss of revenue and triggering an impairment risk for ATC's parent company and resulting in a massive outcry from Serato users).
- 234.6. The foreclosure conduct may breach the law.
235. ATC also submitted that it would not be profitable for it to engage in foreclosure.
- 235.1. Serato users would not be likely to switch to Pioneer DJ and are more likely to be loyal to their hardware and switch software;³⁵⁷ and
- 235.2. []³⁵⁸ []³⁵⁹
236. NERA conducted an assessment of the incentive to foreclose using an analysis known as 'vertical arithmetic'.³⁶⁰
237. There are two steps to the analysis.
- 237.1. By using the relevant margins for DJ hardware and software providers, one can calculate how many customers would need to switch from rival DJ hardware providers to ATC hardware to make foreclosure profitable (this is referred to as the 'critical diversion ratio'). A high critical diversion ratio means that many customers would need to switch from rival DJ hardware providers to ATC to make foreclosure profitable and vice versa.
- 237.1.1. If margins for DJ software are low and margins for DJ hardware are high, then it will be relatively cheap to foreclose. The critical diversion ratio will be low, meaning few customers would need to switch from rival DJ hardware providers to ATC to make foreclosure profitable.
- 237.1.2. If margins for DJ software are high and margins for DJ hardware are low, then it will be relatively expensive to foreclose. The critical diversion ratio will be high, meaning many customers would need to switch from rival DJ hardware providers to ATC to make foreclosure profitable.
- 237.2. Having calculated the critical diversion ratio, one then assesses whether the 'actual diversion ratio' will exceed the critical diversion ratio. That is, we ask

³⁵⁷ ATC "Submission by AlphaTheta Corporation on the Statement of Issues" (8 April 2024) at [8.3]-[8.5].

³⁵⁸ Email from ATC with comments on unredacted SoUI (20 June 2024).

³⁵⁹ Email from ATC with comments on unredacted SoUI (20 June 2024).

³⁶⁰ See for example Simon Bishop and Mike Walker *The Economics of EC Competition Law: Concepts, Applications and Measurement* (Sweet and Maxwell, 2010).

whether enough customers would in fact switch from rival DJ hardware providers to make foreclosure profitable. If the actual diversion ratio is likely to exceed the critical diversion ratio, then it would suggest the merged entity has an incentive to engage in a foreclosure strategy.

238. NERA's main conclusions were that:³⁶¹

238.1. hardware margins are larger than software margins (which 'mechanically' indicates a high incentive to foreclose); and

238.2. the margins differed between expensive (higher absolute margins) and inexpensive hardware (lower absolute margins), meaning the incentive to foreclose was higher for expensive hardware and lower for inexpensive hardware (who NERA claim are the most relevant group to an assessment of foreclosure incentives since they constitute the majority of Serato DJ Pro subscribers).

239. NERA further submitted that:³⁶²

239.1. To implement a foreclosure strategy, ATC would need to compensate Serato for missing out on the earnout (which NERA refers to as 'cashing out' the SPA). ATC would need to recoup the cost of that cash out through foreclosure. This significantly increases the critical diversion ratios [] making it unlikely that ATC would have an incentive to foreclose.

239.2. Foreclosure would harm competition and innovation resulting in the overall market shrinking. This would reduce the incentive to foreclose. NERA submitted that foreclosing rival DJ hardware providers would reduce innovation in that market and shrink the overall size of the market (NERA refers to this as 'dynamic impacts').³⁶³ This would be an additional cost to foreclosure that should be taken account when assessing incentive to foreclose. NERA attempted to estimate these 'dynamic impacts' and estimates that the critical diversion ratio would be between [] (depending on other assumptions).³⁶⁴ That is, between [] of rival DJ hardware customers would need to switch to ATC's Pioneer DJ hardware to make foreclosure worthwhile.

239.3. A large proportion of Serato DJ Lite users do not upgrade to Serato DJ Pro and stop using the software altogether. These users should be excluded from the analysis. Excluding these users significantly increases the critical diversion ratio [] making it unlikely that ATC would have an incentive to foreclose.

³⁶¹ NERA Economic Consulting "AlphaTheta Corporation/Serato: unilateral effects and foreclosure theories of harm" (27 November 2023) at [4(c)(ii)].

³⁶² NERA Economic Consulting "ATC/Serato: Issues raised in the SOI" (8 April 2024).

³⁶³ NERA Economic Consulting "ATC/Serato: Issues raised in the SOI" (8 April 2024).

³⁶⁴ [].

239.4. There are many Serato users that have existing devices who would not be affected by the foreclosure. There would be a delay for the full effects of foreclosure to take place, which reduces the strength of the effect.

240. NERA also submitted that there is less likely to be an ability to foreclose high-end hardware since it often comes with embedded software.³⁶⁵ Moreover, as Pioneer DJ equipment is relatively expensive compared to other DJ hardware providers, Serato customers using inexpensive hardware are more likely to switch software than buy more expensive hardware. This would suggest the actual diversion is low.

Serato's views

241. Serato submitted that it would be unlikely that the Parties would be able to negotiate terms to “cash out” of the SPA.³⁶⁶

241.1. ATC would need to make an exceptionally compelling offer (which is unlikely to be economically rational).

241.2. The vertical arithmetic model does not account for the cost of cashing out (which would greatly increase the cost of foreclosure and so making foreclosure unlikely).

242. Serato also submitted that:³⁶⁷

242.1. There would be significant risks, and only modest gains, from engaging in foreclosure.

242.2. ATC has no incentive to engage in foreclosure conduct, and Serato would not let this happen due to the effect on the earnout (which forms the majority of the payout for the Serato business).

242.3. ATC would therefore not pay to cash Serato out of the SPA provisions to allow it to pursue a vertical foreclosure strategy. The provisions were agreed to in the SPA before the proposed transaction was being investigated by competition authorities, which Serato submitted is reliable evidence of the Parties' intentions.

243. Lastly, Serato submitted that foreclosure would adversely affect its reputation.³⁶⁸

243.1. An important selling point of Serato is broad compatibility. This allows a DJ to show up at a club with confidence they can perform using Serato. If Serato

³⁶⁵ NERA Economic Consulting “AlphaTheta Corporation/Serato: unilateral effects and foreclosure theories of harm” (27 November 2023) at [4(c)(ii)].

³⁶⁶ Serato “Submission in response to Commerce Commission Statement of Issues” (8 April 2024) at [152]-[156].

³⁶⁷ Serato “Submission on Statement of Unresolved Issues” (17 June 2024) at [27]-[28].

³⁶⁸ Serato “Submission in response to Commerce Commission Statement of Issues” (8 April 2024) at [181]-[183].

was to limit that compatibility, this would significantly reduce its reach and generate customer backlash.

- 243.2. Implementing a foreclosure strategy concerning DJ software and hardware would highly likely tarnish the reputation of the merged entity, affecting not just the DJ market but potentially souring its standing within the music production sector.

Our assessment of the merged entity's incentive to foreclose competitors

244. The merged entity would only have an incentive to foreclose if the expected profits gained in the DJ hardware market from foreclosing rival DJ hardware providers exceeds the expected profits lost in the DJ software market.
245. For the reasons set out in detail below, we are not satisfied that ATC would not have the incentive to foreclose competitors in the DJ hardware market. In summary:
- 245.1. we do not think NERA's calculations of the critical diversion ratio can be relied on and the true figure may be much lower; and
- 245.2. while it is difficult to know the 'correct' critical diversion ratio, the actual critical diversion may be relatively high (since there may be many customers of the rival DJ hardware providers that would be willing to switch to ATC's Pioneer DJ products).

The critical diversion ratio is likely lower than NERA estimates

246. NERA calculates the critical diversion ratios using the Parties' data.³⁶⁹ NERA's initial model estimated that the critical diversion ratio including all hardware was moderate at []. However, the critical diversion ratio differed significantly between the types of equipment. For example, the critical diversion ratio was:
- 246.1. relatively small at [] for more expensive hardware such as 'all-in-ones' (that is, indicating a higher incentive to foreclose); and
- 246.2. relatively large at [] for less expensive hardware such as controllers (that is, indicating a lower incentive to foreclose).
247. Our view is that NERA's model has some errors that result in the critical diversion ratios being overstated. Accordingly, we are not able to rely on the figures that NERA have estimated.
248. The main concern we have with the model is that it overestimates the DJ software margin (and therefore underestimates the critical diversion ratios).³⁷⁰ NERA's model

³⁶⁹ NERA Economic Consulting "AlphaTheta Corporation/Serato: unilateral effects and foreclosure theories of harm" (27 November 2023) at [Table 3.4].

³⁷⁰ A related problem is that the NERA also applies the same DJ software margin (assuming all users upgrade to Serato DJ Pro) to all types of hardware regardless of cost. This in part explains why the critical diversion ratio is relatively small for expensive hardware (such as all-in-ones) and relatively high for cheaper

assumes that all users of Serato purchase a subscription to Serato DJ Pro. However, many Serato users only use Serato DJ Lite. We consider that the expected margins should take into account that some buyers of DJ hardware will not purchase a subscription to Serato DJ Pro but will only use Serato DJ Lite.³⁷¹

249. Taking this into account will reduce the expected margin for Serato and reduce the estimated critical diversion ratio. The extent of this depends on the proportion of Serato DJ Lite customers that upgrade to Serato DJ Pro. We believe that [] proportion would be likely to do so. For example []

].³⁷²

].³⁷³ This means the critical diversion ratios for products that only come with Serato DJ Lite are likely to be []. For example, if one (conservatively) assumes that around [] of customers that use Serato DJ Lite will be converted to a paid subscription, NERA's model appears to estimate a critical diversion ratio for an ATC controller of [].³⁷⁴

250. NERA submitted that to implement a foreclosure strategy, ATC would need to compensate Serato for missing out on the earnout ('cashing out'). NERA submitted that ATC would need to recoup the cost of that cash out through the foreclosure strategy. This would significantly increase the critical diversion ratio (the number of customers of non-ATC hardware that would need to switch to Pioneer DJ to make foreclosure profitable) to a level that it is unlikely to achieve.
251. We disagree with NERA's approach because it does not recognise that through 'cashing out' of the SPA, ATC avoids the cost of the earnout. Avoiding the earnout would be a saving for ATC and ignoring this exaggerates the cost that ATC would incur from negotiating a cash out. It is the difference between the cash out and the expected earnout that represents the additional cost that the foreclosure strategy would need to recoup.

251.1. If the cash out was greater than the expected earnout then it would represent an additional cost for ATC to recoup and therefore reduce the incentive to foreclose. In this case the cost to be recouped would be the

hardware (such as controllers). In reality customers of higher priced DJ hardware are more likely to use Serato DJ Pro software (which often comes in a bundle with the DJ hardware) and customers of lower priced DJ hardware are more likely to use Serato DJ Lite. Changing the model to reflect this means the difference in critical diversion ratio between 'all-in-ones' and controllers is not so great.

³⁷¹ Following feedback, NERA provided updated figures setting out a range of critical diversion ratios that depended on the proportion of customers that upgrade to Serato DJ Pro. As noted, we consider that the evidence suggests a [] proportion of customers take up Serato DJ Pro and therefore the critical diversion ratios are likely to be towards the [] bound of the range that NERA estimated.

³⁷² For example, in the calendar 2022 Serato sold [] DJ hardware units with Serato DJ Lite, but Serato increased its subscriber numbers by about []. This suggests only around [] were converted to Serato DJ Pro (Serato RFI response (7 November 2023)).

³⁷³ [].

³⁷⁴ [].

difference between the cash out and the expected earnout (rather than the full cash out as the Parties suggest).

251.2. If the cash out was the same as what ATC expects to have paid under the earnout, ATC would face no additional cost to a foreclosure strategy.

251.3. If the cash out turned out to be less than the expected earnout, then it would represent a cost saving to ATC which would increase the incentive to foreclose.³⁷⁵

252. NERA argued that the cash out is an additional cost.³⁷⁶ NERA's reasoning is that ATC was only willing to pay a certain value upfront (USD\$65million) and therefore ATC's expectation of the value of the earnout payments is zero. Accordingly, NERA claims the cash out would represent an additional cost that would need to be recouped if ATC engaged in foreclosure. We do not accept this argument. Just because ATC was only willing to pay USD\$65million upfront does not imply that was all it was expecting to pay. That would only be the case, if ATC expected to pay nothing for the earnout. For the earnout to be zero would require that []³⁷⁷ We do not think it realistic that ATC would have that expectation.

252.1. Serato's projected [] Serato included in its management presentation to potential buyers projections of []³⁷⁸ []
].

252.2. An ATC internal document, used to justify the purchase of Serato, []³⁷⁹ ATC itself stated in the Application that the earnout is expected to represent a material proportion of the consideration.³⁸⁰

253. We also disagree with NERA's other arguments.

253.1. NERA submitted that the vertical arithmetic model does not take into account the cost from 'dynamic impacts' of foreclosure. That is, that foreclosure

³⁷⁵ As we note earlier, it is possible that ATC could engage in conduct where the breach is uncertain. While Serato may be eligible for contractual damages, if there is uncertainty over whether a breach occurred, the damages may be less than what ATC would need to pay under the earnout.

³⁷⁶ NERA Economic Consulting []
³⁷⁷ []

³⁷⁸ []
³⁷⁹ []

³⁸⁰ The Application at [3.2].

would harm innovation, which would shrink the market and reduce growth for the merged entity. NERA provided estimates on how the critical diversion ratio might be affected taking into account the 'dynamic impacts' of a foreclosure strategy. While we recognise that foreclosure could adversely affect market growth, we do not find NERA's estimates on the size of the impact to be persuasive.

253.1.1. NERA's model suggests the 'dynamic impacts do not make much difference to the incentive to foreclose. It has modelled dynamic impacts by assuming a reduction in Serato's forecasted revenue growth of 25%, 50% and 75% (these values appear to be arbitrary, NERA does not indicate which of these is the most likely). However, even using 75% changes the critical diversion ratio by only a few percentage points.

253.1.2. NERA's model starts with an assumption that the full cash out amount is a cost of foreclosure. As we explain above, we consider this overestimates the cost of foreclosure and inflates the critical diversion ratios.

253.2. We do not agree that it is appropriate to exclude certain users of Serato DJ Lite from the calculations. Serato earns revenue on all customers that purchase a device with Serato DJ Lite through royalty and integration fees, regardless of whether these customers will continue to use Serato into the future. As such, they represent a potential loss to Serato that should be accounted for in the model. If they are unlikely to switch to ATC hardware, this should be taken account in the assessment of actual diversion (not the critical diversion).

253.3. Some customers who already own devices (or who buy existing devices already on the shop floor) may not be affected by foreclosure. However, innovation is a source of competition in the market and hardware providers frequently release new products.³⁸¹ The foreclosure strategy could adversely affect the constraint imposed by new releases of ATC's DJ hardware rivals.

The actual diversion ratio may exceed the critical diversion ratio

254. The next step in a vertical arithmetic model is to test whether the actual diversion ratio will exceed the critical diversion ratio. As noted, the actual diversion ratio is the number of customers that would switch from rival DJ hardware providers to ATC's hardware if Serato's DJ software no longer worked with the rival DJ hardware. A customer is more likely to switch if:

254.1. they want to continue using Serato's DJ software; and

³⁸¹ For example, recent releases by hardware producers include ATC's Omnis-Duo all-in-one system and DDJ-REV5 controller.

- 254.2. ATC can offer DJ hardware that is sufficiently attractive to the customer.
255. We do not know what the actual diversion ratio is because we do not have robust data on how customers of rival DJ hardware providers would respond to a foreclosure strategy, in particular the extent to which they would switch to ATC's products. However, we consider that the actual diversion ratio could exceed reasonable estimates of the critical diversion ratio.
- 255.1. First, Serato's DJ software is very popular with customers of DJ hardware and the evidence shows that there is strong customer inertia which limits switching to other DJ software providers (see paragraph [191]). Serato's revenues have [].³⁸² Therefore, we think there is a real chance that a large proportion of customers of rival DJ hardware providers will continue using Serato's DJ software and thus switch to ATC.
- 255.2. Second, ATC supplies the leading brand of DJ hardware (Pioneer DJ). We estimate Pioneer DJ has a [] share of the controller market (around []). Market share is not always a good indicator of diversion in markets where there are differentiated products. However, ATC has products at a wide range of price points and the evidence suggests that many customers of rival DJ hardware providers would view ATC's products as a good alternative to their existing products.
256. NERA submitted that customers that purchase non-ATC hardware with Serato DJ Lite are unlikely to switch to ATC hardware because Serato DJ Lite is targeted at beginner DJs who use inexpensive hardware and are unlikely to switch to ATC hardware which is more expensive.³⁸³ However, we are not satisfied that this is likely to be the case.
- 256.1. We do not think one can assume that users of Serato DJ Lite do not strongly value being able to use that software. Even though it is free, users may develop a preference for using Serato and therefore on their next purchase will seek a DJ hardware device that can be used with Serato.³⁸⁴ Users may also desire to use Serato DJ Lite as they may have ambitions to start playing in clubs, at which time they will subscribe to Serato DJ Pro.
- 256.2. Pioneer DJ offers products at a wide range of price points, including products towards entry level.³⁸⁵ Furthermore, given Pioneer DJ's popularity (as illustrated by its market share), many customers that purchase entry-level

³⁸² See for example [].

³⁸³ [].

³⁸⁴ If the customer switches DJ hardware at the end of the life of their existing device, the customer will not incur any additional financial cost from switching compared to continuing with the same DJ hardware brand.

³⁸⁵ For example, on the Rockshop's website, the cheapest Pioneer is NZD\$399 (DDJ-200). <rockshop.co.nz> available 29 July 2024. The DDJ-200 is marketed as a "beginner DJ controller". <pioneer.co.nz> available at 2 August 2024. In comparison, the lowest priced Numark controllers are NZD\$149 (Numark DJ2GO2), NZD\$249 (Numark Party Mix II MK2) and NZD\$300 (Numark Party Mix Live). The cheapest Native Instrument controller is NZD\$369 (Traktor Kontrol Z 1). The cheapest Roland is NZD\$499 (Roland DJ-202).

hardware may well be willing to pay any extra required to buy a Pioneer DJ controller.

257. ATC submitted that it has no history of attempting to foreclose competitors. Even if this is true, ATC's incentives to foreclose may change as a result of acquiring Serato. ATC also submitted that it would not be consistent with its plans for Serato and that growing DJ software was as important as ATC's DJ hardware strategy. The evidence we have viewed leaves the Commission not satisfied that ATC would not have the incentive to foreclose DJ provider competitors. Accordingly, we are not able to rely on such statements as to future conduct.

Other factors are unlikely to prevent foreclosure

258. We are not satisfied that ATC would be disincentivised from engaging in foreclosure because of any impact on ATC's reputation.³⁸⁶

258.1. We recognise that some types of foreclosure strategies could adversely affect ATC's reputation (such as immediately ending interoperability for all products). However, ATC could engage in partial foreclosure strategies that are not so obvious such as making the process of integration with rival DJ hardware providers longer or less complete which would result in less reputational damage than total foreclosure.

258.2. We do not agree that foreclosure would necessarily have the negative financial consequences arising from a loss in value of Serato that ATC suggests. Our analysis suggests that foreclosure may be profitable and therefore enhance ATC's value.

258.3. Serato raised concerns that foreclosure would mean DJs would be in doubt whether they could use Serato when they arrive at a club. We understand that Pioneer DJ equipment is commonly used in clubs.³⁸⁷ The foreclosure could have the impact of reinforcing Pioneer DJ's position in clubs. That is, clubs may be even more likely to choose Pioneer DJ in future to ensure the hardware is compatible with Serato.

259. We do not consider that there are other factors that would constrain the merged entity from engaging in foreclosure. As discussed earlier, we are not satisfied that any legal requirements on ATC to continue to supply Serato to its hardware rivals would be sufficient to prevent foreclosure, including the Commerce Act (which only

³⁸⁶ For example, [] noted that if ATC did try to prevent integration, there would likely be some negative reaction, but the question would be how long that would last. [] said that it expects there would be a short period of negativity, but public sentiment would then revert to normal (Commerce Commission interview with []).

³⁸⁷ For example, [] said that Pioneer owns the club space (Commerce Commission interview with []). [] estimated that around 70-75% of clubs used Pioneer equipment (Commerce Commission interview with []). [] said that Pioneer gear is typically found in clubs in Auckland and Wellington (Commerce Commission interview with []).

prohibits such conduct where, as assessed in the post-merger markets, with increased concentration, it results in a substantial lessening of competition).

Impact of foreclosure on competition in the DJ hardware market

260. We consider that the competition lost from potentially foreclosed DJ hardware competitors would be sufficient to have the likely effect of substantially lessening competition in the DJ hardware market.

ATC's views

261. ATC submitted that the five years during which the SPA provisions apply will provide rival hardware manufacturers with more than sufficient time to develop their own DJ software, invest to improve their own existing DJ software or partner with other DJ software providers to provide a bundled offering.³⁸⁸

Serato's views

262. Serato submitted that a foreclosure strategy would take a long time to implement, which would give rival hardware providers time to protect themselves against a foreclosure strategy by:³⁸⁹

262.1. Progressing their integration of other DJ software offerings, including mobile apps. Serato said that this would provide the greatest protection against a foreclosure strategy. An important selling point of Serato is broad compatibility. This allows a DJ to show up at a club with confidence they can perform using Serato. If Serato was to limit that compatibility, this would significantly reduce its reach and generate customer backlash.

262.2. Developing their own DJ software offering, similar to ATC's development of rekordbox. Serato said that DJ hardware providers could have success in doing this if they are willing to make the right investments in marketing and take advantage of their existing strengths and routes to market.

263. Serato said that DJ hardware providers would have 10 years to enact these strategies, given the five-year protection provided in the SPA and the 3-5 year lifespan of DJ hardware (as Serato said that it would not withdraw support for hardware once it has been manufactured).³⁹⁰

Our assessment of the impact of foreclosure on competition

264. We consider that any foreclosure of DJ hardware providers is likely to impact competition.

265. We are not satisfied that there would be any effective counterstrategies that DJ hardware rivals would be able to employ to defeat the foreclosure:

³⁸⁸ ATC "Submission by AlphaTheta Corporation on the Statement of Issues" (8 April 2024) at [7.57(c)].

³⁸⁹ Serato "Submission in response to Commerce Commission Statement of Issues" (9 April 2024) at [167]-[170].

³⁹⁰ Serato "Submission in response to Commerce Commission Statement of Issues" (8 April 2024) at [170].

265.1. For reasons we discuss earlier at paragraphs [184]-[196], it is unlikely that hardware rivals would be able to develop their own software in the short term due to the barriers to entry and expansion:

265.1.1. Serato has been developed over many years. It is likely that developing an equivalent software would be costly and time consuming, without any guarantee that customers will accept the software.

265.1.2. Market participants have indicated that DJs are reluctant to switch between software providers.

265.2. It is unlikely that rival DJ hardware suppliers would be able to compete effectively by partnering with or acquiring another software provider. As noted above, the evidence does not suggest there are any other software providers that have the same brand strength as Serato. rekordbox might have been an attractive DJ software for DJ hardware providers to partner with but (as noted above) we would not expect ATC to offer rekordbox for integration if it chooses a foreclosure strategy.

266. We are also not satisfied that there are any efficiencies or new innovations that could emerge that would offset the harm to competition in the DJ hardware market. Further, given our conclusion on unilateral effects, it is unclear any efficiencies – to the extent they are realised – would be passed on to consumers.

Foreclosure in the DJ hardware market at the end of the SPA

267. We consider that the merged entity is likely to have the ability and incentive to foreclose competitors in the DJ hardware market once the protections of the SPA have ended and that this would amount to a substantial lessening of competition in that market.

ATC's views

268. ATC submitted that the DJ industry will see significant technological change in the next 3-5 years and that, as a result, by the time the provisions in the SPA expire, the competitive landscape of the industry will have changed.³⁹¹

269. ATC argued that, due to these anticipated market changes, Serato is unlikely to be essential by the time the SPA provisions expire.³⁹²

269.1. Serato does not have a mobile app, meaning it is behind its competitors who have already invested in developing an app;

³⁹¹ ATC "Submission by AlphaTheta Corporation on the Statement of Issues" (8 April 2024) at [7.56].

³⁹² ATC "Submission by AlphaTheta Corporation on the Statement of Issues" (8 April 2024) at [7.57].

- 269.2. DJ hardware with embedded software, such as CDJs and all-in-ones, is increasing and this will reduce the demand for standalone software such as Serato; and
- 269.3. the Contingent Consideration Period will enable rival hardware manufacturers with sufficient time to develop competitive software products.

Serato's views

270. Serato submitted that the DJ industry is dynamic and constantly changing in response to external innovations and innovations by market participants. Serato states that it expects the next five years will see significant change.³⁹³
271. Serato illustrated this by providing examples of changes in the DJ industry since July 2023, including:³⁹⁴
- 271.1. Reelock launching a 4 channel mixer primarily for Algoriddim;
- 271.2. Algoriddim djay launching its integration with Apple Music;
- 271.3. the release of Engine DJ 3.4, which includes Bluetooth audio;
- 271.4. Mixxx releasing the latest version of its DJ software which includes support for Apple Silicon; and
- 271.5. Denon releasing DMX lighting support for Prime 4+.
272. Serato argued that it does not consider its software to be “must have” today and that its products are likely to be even further from a “must have product” after the Contingent Consideration Period expires on 31 December 2028, because:³⁹⁵
- 272.1. mobile apps already provide a strong constraint;
- 272.2. the popularity of embedded hardware such as CDJs and all-in-ones is likely to increase;
- 272.3. the cost of embedded DJ hardware may start to decrease as hardware advances, resulting in increased focus on these products by consumers and manufacturers;
- 272.4. DJ hardware competitors will likely release their own DJ software;
- 272.5. the boundaries between DJing, music production and live performance are increasingly blurring, and demand may shift to comprehensive music creation products; and

³⁹³ Serato “Submission in response to Commerce Commission Statement of Issues” (8 April 2024) at [184].

³⁹⁴ Serato “Submission in response to Commerce Commission Statement of Issues” (8 April 2024) at [185], where the full list of innovations noted is available.

³⁹⁵ Serato “Submission in response to Commerce Commission Statement of Issues” (8 April 2024) at [186].

272.6. artificial intelligence and machine learning could revolutionise the DJ software industry by offering new features.

Our assessment of the potential for foreclosure at the end of the SPA earnout period

273. We are not satisfied that a substantial lessening of competition in the DJ hardware market due to potential foreclosure is not likely once the SPA protections have expired.
274. As noted above, we usually assess competition effects over the short term (ie, two years). The relevant timeframe for assessment will, however, depend on the circumstances. A longer timeframe will be appropriate if, on the evidence, competition effects are likely to arise in later years.³⁹⁶
275. For example, long term supply arrangements, or events such as COVID, can mean that competition effects may not be felt for some years into the future, and justify a longer-term assessment.³⁹⁷
276. Notwithstanding our view that the merged entity has the incentive and ability to foreclose DJ hardware competitors despite the provisions in the SPA to the Proposed Acquisition, not all competition impacts may be felt until after the Contingent Consideration Period expires. We have therefore considered the likelihood of foreclosure occurring following the expiration of the Contingent Consideration Period. This means we have looked forward to assess the risk of foreclosure occurring from 1 January 2029.
277. We acknowledge the Parties' submissions that the market is dynamic and subject to technological change. We do not, however, accept that these dynamics mean that:
- 277.1. Serato does not have market power for software products for DJ hardware providers; and
- 277.2. there is not a real chance that Serato will not have substantial market power for DJ software as of 1 January 2029.
278. Serato has maintained its position as the leading DJ software product despite the technological changes that have occurred in the market over recent years. We have not seen evidence to demonstrate that its resilience to these market dynamics is likely to fall away in the coming years. As we note earlier, we are not satisfied that new entry or expansion is likely. This is because barriers to entry or expansion such as such as the time and cost of developing DJ software, coupled with difficulties in getting customers to switch DJ software providers, appear significant.
279. We also consider some of Serato's arguments to be speculative (for example, Serato argued that artificial intelligence and machine learning 'could' revolutionise the DJ

³⁹⁶ *Woolworths & Ors v Commerce Commission* (HC) above n8 at [131].

³⁹⁷ See, for example, *THL Group (Australia) Pty Limited and Apollo Tourism & Leisure Ltd* [2022] NZCC 32 at [28], and *Connexa Limited and Two Degrees Networks Limited and Two Degrees Mobile Limited* [2023] NZCC 10 at [78].

software industry and that demand ‘may’ shift to comprehensive music creation products). We were not provided with evidence in support of these arguments.

280. As a result, we are not satisfied that that ATC will not engage in foreclosure of rival DJ hardware competitors who currently partner with Serato, subsequent to the Contingent Consideration Period.

Ability and incentive to foreclose DJ software competitors

ATC’s views

281. ATC submitted that the Proposed Acquisition would not give it any greater ability or incentive to foreclose competition in the DJ software market than it has currently. ATC stated that:³⁹⁸

281.1. it already has its own DJ software products, and if it was profitable (and possible) to refuse to allow rival DJ software to be used with its DJ hardware, it would already be doing so; and

281.2. the ability to MIDI map would allow consumers to use rival DJ software products with ATC’s DJ hardware products.

282. ATC further submitted that it does not have the ability to foreclose since:³⁹⁹

282.1. a high market share, particularly in a dynamic market, does not necessarily indicate substantial market power; and

282.2. DJ software providers already have the technological capability to make their software compatible with ATC’s hardware without any support from ATC, and the same providers will also be able to counter any preventative measures ATC may attempt.

283. ATC submitted that it would not have the incentive to foreclose since it would be profitable to ensure widespread use of its products.⁴⁰⁰

284. NERA’s report in support of ATC’s Application conducted vertical arithmetic found it was unlikely the merged entity would have the incentive to implement a foreclosure strategy in the DJ software market.⁴⁰¹

Serato’s views

285. Serato submitted that it is not correct that existing DJ software competitors need to grow before they become viable partners for DJ hardware competitors because DJ software competitors are already at a viable scale, DJ software competitors are

³⁹⁸ The Application at [7.35]-[7.36].

³⁹⁹ ATC “Submission by AlphaTheta Corporation on the Statement of Issues” (8 April 2024) at [9.1]-[9.6].

⁴⁰⁰ ATC “Submission by AlphaTheta Corporation on the Statement of Issues” (8 April 2024) at [9.2].

⁴⁰¹ NERA Economic Consulting “AlphaTheta Corporation/Serato: unilateral effects and foreclosure theories of harm” (27 November 2023) at [4(d)].

already able to map to DJ hardware providers without assistance and it is unlikely that competitors could be pushed below a viable scale.⁴⁰²

Our assessment

286. In our view, ATC may have the ability to foreclose DJ software competitors. Table 2 below sets out our estimate of global market shares for the supply of DJ controllers and all-in-one units.

Table 2: Estimates of DJ hardware market shares based on units

Name	CY2020		CY2021		CY2022	
	# units ('000)	Market share (%)	# units ('000)	Market share (%)	# units ('000)	Market share (%)
ATC	[
inMusic						
Reloop						
Roland						
Native Instruments						
<i>Total</i>]

*Source: Information provided by the market participants.
Note: Individual figures may not add to total due to rounding.*

287. ATC submitted that market share alone is not sufficient to conclude that a firm has market power. We agree. However, ATC seems to have held that market share over a long period and has strong brand recognition, which suggests it has market power.
288. Despite ATC's argument that if it was profitable (and possible) to refuse to allow rival DJ software to be used with its DJ hardware, it would already be doing so, the evidence we received from market participants suggests it would be technically feasible for ATC to prevent DJ software from interoperating with DJ hardware []].

288.1. One software provider noted that DJ hardware providers can implement technical measures to restrict access of third-party software developers.⁴⁰³ []].

⁴⁰² Serato "Submission in response to Commerce Commission Statement of Issues" (8 April 2024) at [189]-[192].

⁴⁰³ []].

].⁴⁰⁴ [

].⁴⁰⁵ [

].⁴⁰⁶

288.2. Another software provider said that DJ hardware providers could insert an artificial block such as an encryption that would prevent integration of its software with the provider’s DJ hardware, although providers could not encrypt hardware devices that use MIDI integration.⁴⁰⁷ This software provider said it is “very afraid” that ATC could want to close off its access to Pioneer DJ hardware.⁴⁰⁸ As an estimated [] of its users use the software with Pioneer DJ hardware, being cut-off from that hardware would cause it to lose a lot of its customers. The software provider said ATC locking out all DJ software competitors would effectively “kill” the competitors and any future innovation.⁴⁰⁹ Such conduct would prevent developers being incentivised to create DJ software because most DJs appear to want to buy Pioneer DJ hardware.

288.3. One of [] concerns with the Proposed Acquisition is ATC preventing [] software from being compatible with Pioneer DJ hardware. [] told us that this would have a “massive impact” and be the “worst case” scenario.⁴¹⁰ It also told us that it has had experience with being [

].⁴¹¹

288.4. If it was not possible for these DJ software providers to be prevented from interoperating with DJ hardware, they would not have expressed these concerns to us.⁴¹²

404 [].

405 [].

406 [].

407 Commerce Commission interview with [].

408 Commerce Commission interview with [].

409 Commerce Commission interview with [].

410 Commerce Commission interview with [].

411 Commerce Commission interview with [].

412 Commerce Commission interviews with [] and []. [].

288.5. ATC has restricted its rekordbox Free software to Pioneer DJ devices, which it said it has done [].⁴¹³

288.6. Although Serato said competitors do not need integration with ATC to reach sufficient scale, as we identified earlier the evidence suggested the inability to reach around [] of the market⁴¹⁴ would affect the decision to enter and invest in expansion in a market. While there may be niche entry, it is unclear that such entry would be sufficient to be a good alternative to Serato.

289. We are not satisfied that ATC would have the incentive to foreclose DJ software competitors as a standalone strategy. This is because as the evidence we gathered suggests that the margin on DJ hardware sales is high when compared to that of DJ software, a large proportion of customers would need to be recaptured by ATC to make software foreclosure profitable.

290. However, we are not satisfied that ATC would not be incentivised to foreclose competition in the DJ software market to support other strategies.

291. First, ATC may be incentivised to foreclose competition in the DJ software market, in conjunction with, and to support, foreclosure of DJ hardware competitors.

291.1. A means through which DJ hardware competitors could try to avoid the foreclosure may be to partner with a DJ software provider or to form a vertically integrated hardware-software company.

291.2. There is a high fixed and sunk cost involved in developing software. An important means to get the scale required to achieve a sufficient return on that cost is to ensure software is available to as many DJs as possible. ATC could raise barriers to entry by refusing to interoperate its hardware with the software of competitors. Those DJ software competitors may then be prevented from reaching scale to become a viable competitor, denying DJ hardware competitors an option to partner with.

292. As we noted above, if this was to occur, it would likely harm the ability of DJ software providers to compete and would limit the DJ software choices available to DJs.

293. Second, as we note in the unilateral section, ATC may also be incentivised to raise barriers to enable it to exercise unilateral market power gained as a result of the Proposed Acquisition.

Competition analysis – access to sensitive information

294. A merger or an acquisition that results in the merged entity accessing sensitive information of competitors could substantially lessen competition. For example, accessing such information could adversely affect competitors' incentives or abilities

⁴¹³ ATC RFI response (17 June 2024).

⁴¹⁴ See Table 2 above.

to compete aggressively or innovate, and thereby reduce the constraint the competitors impose.⁴¹⁵

295. In this case the concern arises out of the vertical relationship between ATC and Serato from the Proposed Acquisition. The concern we have tested is as follows.
- 295.1. As part of the integration process, Serato obtains sensitive information from DJ hardware providers.
- 295.1.1. DJ hardware providers that integrate their hardware with Serato software need to provide the unreleased hardware to Serato in advance of a product's launch in order to ensure that compatibility. During this process, the DJ hardware providers hand over to Serato their unreleased product ideas, including new design features or hardware features. We understand that part of this process is collaboration between the DJ hardware and software providers around how the hardware works with the software.
- 295.1.2. Serato receives access to sensitive information about users of DJ hardware providers post-hardware launch, such as how the software is being used with the hardware and user information (eg, location).
- 295.2. If, due to the vertical integration from the Proposed Acquisition, ATC got hold of this information it could harm competition.
- 295.2.1. DJ hardware rivals may have less of an incentive to innovate knowing there is a risk that ATC could appropriate those ideas. If the DJ hardware rivals know that ATC could obtain those ideas, this may weaken the incentive to innovate in the first place and harm competition. Rival DJ hardware providers may be less willing to work with Serato if they feared ATC could access sensitive information about their customers.
- 295.2.2. Similarly, ATC may reduce its efforts to innovate and offer less competitive products. This is because it will be better informed about its rivals' planned products and face less risk from failing to keep up with competitor innovations.
296. For the reasons we set out below, we are not satisfied that the Proposed Acquisition will not have, or would not be likely to have, the effect of substantially lessening competition in the DJ hardware market due to the merged entity's access to the sensitive information of its DJ hardware competitors' post-acquisition.

⁴¹⁵ Access to sensitive information could also facilitate coordination between the merged entity and competitors, although in this case we do not see the Proposed Acquisition materially increasing the risk of coordination. There are significant differences in size and structure between competitors in the DJ hardware market, and their products are not homogenous. This makes it less likely that the market participants will have aligned incentives to coordinate.

ATC's views

297. ATC submitted that there will be measures in place to protect its DJ hardware competitors' sensitive information, including:⁴¹⁶
- 297.1. Serato implementing a confidentiality protocol (Protocol) post-acquisition to protect its DJ hardware partners' confidential information (in addition to Serato's existing confidentiality obligations with individual DJ hardware partners);
 - 297.2. ATC offering to enter into individual agreements with DJ hardware partners to appropriately safeguard any confidential information provided to Serato within the Serato business without interference from ATC; and
 - 297.3. the SPA provisions "comprehensively" addressing any risk of ATC using DJ hardware competitors' confidential information. ATC submitted that if it were to breach these provisions, DJ hardware competitors are likely to end their partnering arrangements with Serato or take legal action against Serato for breaching the relevant partnering agreement(s), hardware protocols and/or non-disclosure agreements (NDAs).

Serato's views

298. Serato submitted that [

].⁴¹⁷ Further, users can [
].⁴¹⁸

299. Serato also noted that:

- 299.1. hardware prototypes would only need to be shared with Serato for software integration as late as two months prior to launch,⁴¹⁹ and
- 299.2. from its perspective, the way the industry operates is that nobody copies a prototype without first seeing how it performs, because no one knows whether a new idea is going to gain traction.⁴²⁰

300. In support of this argument, Serato referenced ATC's statement that [

].⁴²¹ [

⁴¹⁶ ATC "Submission by AlphaTheta Corporation on the Statement of Issues" (8 April 2024) at [10.4]-[10.6].

⁴¹⁷ Serato "Submission in response to Commerce Commission Statement of Issues" (8 April 2024) at [217].

⁴¹⁸ Serato "Submission in response to Commerce Commission Statement of Issues" (8 April 2024) at [217].

⁴¹⁹ Serato "Submission in response to Commerce Commission Statement of Issues" (8 April 2024) at [202].

⁴²⁰ Serato "Submission on Statement of Unresolved Issues" (17 June 2024) at [33].

⁴²¹ Serato "Submission on Statement of Unresolved Issues" (17 June 2024) at [35].

].⁴²²

301. Serato submitted that there will be sufficient measures to protect DJ hardware competitors' planned innovations, customer information and incentives to compete, and to protect against the risk of coordination.⁴²³

301.1. Serato has developed information protocols to apply to any information hardware providers choose to share with Serato prior to launch. The protocols include Serato maintaining an operational board that will be entirely separate from the ATC board, as well as IT, physical and operational security obligations to protect hardware partners' confidential information.⁴²⁴

301.2. Serato submitted that vertically integrated business models are commonplace in competitive markets and that many firms compete with their suppliers or customers in upstream or downstream markets.⁴²⁵ Where this occurs, Serato said that information sharing protocols are frequently used to record the importance of not sharing commercially sensitive information received by a business with the parts of the business that compete with the supplier of the information. Serato also said there is no basis for a theory of harm that vertical integration in this case would be likely to lessen competition in any market.⁴²⁶

302. Serato told us that the protocols and the legal frameworks in place ensure that the confidential information remains protected, preventing any potential conflicts of obligation for Serato's operationally separate board members.⁴²⁷

302.1. [

302.2.

302.3.

].

⁴²² ATC RFI response (5 July 2024).

⁴²³ Serato "Submission in response to Commerce Commission Statement of Issues" (8 April 2024) at [193].

⁴²⁴ Serato "Submission in response to Commerce Commission Statement of Issues" (8 April 2024) at [209].

⁴²⁵ Serato "Submission on Statement of Unresolved Issues" (17 June 2024) at [30].

⁴²⁶ Serato "Submission on Statement of Unresolved Issues" (17 June 2024) at [30].

⁴²⁷ Serato RFI response (20 June 2024).

303. Serato is [].

304. Serato also said [].⁴²⁸

304.1. The type of information to be shared with Serato will depend on the DJ hardware partner's chosen level of Serato's involvement in the development of a new hardware and, according to Serato, even active involvement from Serato requires limited information sharing.⁴²⁹ Serato also noted that DJ hardware partners that choose to limit the information shared with Serato will not experience significant competitive disadvantage.⁴³⁰

304.2. DJ hardware partners have other protective measures within their control, including implementing the Protocol, partnering with other software providers or limiting the information they share with Serato (eg, by involving Serato after a product's launch or announcing a new piece of hardware before it becomes available).⁴³¹

305. Regarding the Protocol with DJ hardware partners, Serato also said that:⁴³²

305.1. [

305.2.

305.3.

305.4.

⁴²⁸ Serato RFI response (20 June 2024).

⁴²⁹ Serato "Submission in response to Commerce Commission Statement of Issues" (8 April 2024) at [195]-[203].

⁴³⁰ Serato "Submission in response to Commerce Commission Statement of Issues" (8 April 2024) at [215].

⁴³¹ Serato "Submission in response to Commerce Commission Statement of Issues" (8 April 2024) at [208]-[212].

⁴³² Serato RFI response (20 June 2024).

305.5.

].

306. Serato further submitted that the Protocol is not intended to be an “entrenched legal masterpiece” but is instead designed to provide commercial comfort to Serato’s DJ hardware partners that their information will be kept confidential.⁴³³ According to Serato, the important consideration is whether the information is materially sensitive from a competition perspective.⁴³⁴ Serato reiterated that the only information it considered that a DJ hardware partner needs to share that would qualify as this sort of information is the hardware prototype (which it said no one would copy without first seeing how the device performs in the market).⁴³⁵

307. Lastly, [

].⁴³⁶

Our assessment of ATC’s access to sensitive information post-acquisition

308. The Parties have submitted that the DJ software and DJ hardware markets are dynamic, where constant technological innovation is critical to long term commercial viability. We have assessed Serato’s submissions regarding the exchange of sensitive information, outlined above, with this context in mind.

The information exchanged during the integration process is commercially sensitive

309. Although Serato considers that there is limited commercially sensitive information from a competition perspective that is exchanged during the DJ hardware integration process with Serato, we note that:

309.1. DJ hardware providers have consistently expressed the opposite view. [] told us that there is value in having a working relationship with Serato, and that the integration process can involve back and forth discussions over a year in advance of a product’s release.⁴³⁷ One hardware provider described the integration relationship as a “synergistic partnership” and said that when Serato provides advice on a particular feature, it listens to what Serato has to say.⁴³⁸ Another said that the software development team at Serato is “crucial” to the product, with the integration process involving collaboration and the sharing and evaluating of concepts and ideas.⁴³⁹ We consider that the evidence provided by these DJ hardware providers, who are

⁴³³ Serato “Submission on Statement of Unresolved Issues” (17 June 2024) at [31].

⁴³⁴ Serato “Submission on Statement of Unresolved Issues” (17 June 2024) at [32].

⁴³⁵ Serato “Submission on Statement of Unresolved Issues” (17 June 2024) at [33].

⁴³⁶ Serato RFI response (20 June 2024).

⁴³⁷ Commerce Commission interviews with [] and [].

⁴³⁸ Commerce Commission interview with [].

⁴³⁹ Commerce Commission interviews with [].

the ones relinquishing control of their sensitive information, is more persuasive than Serato’s views on how sensitive the information is.

- 309.2. One hardware provider told us that every piece of information shared during that process is commercially sensitive,⁴⁴⁰ while another told us that the information provided to Serato during the integration process is its “absolute strategy” for taking on the competition.⁴⁴¹ Both hardware providers agreed that there would not be a way to retain the same level of integration with Serato without providing as much commercially sensitive information.⁴⁴²
- 309.3. inMusic submitted that it provides hardware designs to Serato many months or even over a year in advance of the product’s launch.⁴⁴³ inMusic said that a lengthy integration process is not necessary for simpler, entry level products, but is necessary to ensure deeper integration that customers can require.
- 309.4. inMusic also submitted that providing Serato with prototypes or designs just before or after launch would not be a viable commercial strategy, particularly because ATC will be able to continue to provide its software to Serato ahead of release, which it may benefit from.⁴⁴⁴ ⁴⁴⁵ inMusic submitted that going forward, it would have to decide between protecting confidentiality (and launching a product without Serato integration, potentially affecting sales numbers) or launching a better product with Serato integration (and risk ATC knowing its new features prior to release).⁴⁴⁶
- 309.5. Continued technological innovation is important to commercial success in the DJ hardware markets. ATC is by the far the largest provider of DJ hardware (around [] share of supply) and [] have all identified they compete directly against ATC.⁴⁴⁷ In this scenario, even small exchanges of competitively sensitive information, over a prolonged period, may confer to ATC a marked advantage.

310. []

⁴⁴⁰ Commerce Commission interview with [].

⁴⁴¹ Commerce Commission interview with [].

⁴⁴² Commerce Commission interviews with [] and [].

⁴⁴³ inMusic “Submission on Statement of Unresolved Issues” (13 June 2024) at [5(f)].

⁴⁴⁴ inMusic “Submission on Statement of Unresolved Issues” (13 June 2024) at [5(f)].

⁴⁴⁵ [] also noted that this would not be a viable strategy, as the product wouldn’t be as successful. [] said that part of the integration process is collaborating in designing the hardware so that its features work with the software (and vice versa) and releasing the hardware and software as a package. This would not be achieved if the integration occurs post-launch. Commerce Commission interview with [].

⁴⁴⁶ inMusic “Submission on Statement of Unresolved Issues” (13 June 2024) at [5(f)].

⁴⁴⁷ Commerce Commission interviews with [], [] and [].

].

310.1. [

].⁴⁴⁸ [

].⁴⁴⁹ [

].⁴⁵⁰

310.2. [

].⁴⁵¹ [

].

310.3. The further information ATC provided about this integration process supports third party DJ hardware providers' comments that deeper integration requires a longer integration period. For example, ATC told us that [

].⁴⁵²

The Protocol proposed by Serato does not address our concerns

311. Generally, the Commission will place weight on the terms of contractual arrangements struck in a bid to assuage competition concerns that arise in a merger context. In order to do so, however, the Commission will consider in detail key aspects of the contractual arrangements.

312. We consider that the Protocol has material limitations.

312.1. [

312.1.1.

⁴⁴⁸ Email from [].

⁴⁴⁹ Email from [].

⁴⁵⁰ Email from [].

⁴⁵¹ Email from [].

⁴⁵² ATC RFI response (5 July 2024).

312.1.2.

]. [

].

312.2. [

312.3.

312.3.1.

312.3.2.

312.4.

].

313. [

].⁴⁵³

313.1. [

⁴⁵³ We were not able to confirm this with [], as [] has not been willing to speak with us throughout this process.

].⁴⁵⁴

313.2. [

].⁴⁵⁵

313.3. [

]. [

].⁴⁵⁶

314. On balance, the submissions made by the Parties regarding the Protocol have not satisfied us that the competition concerns regarding ATC's access to sensitive information of Serato's DJ hardware partners are unlikely arise in the factual.
315. For completeness, we also find it difficult to place weight on ATC's offer to enter into individual agreements with Serato's DJ hardware partners to appropriately safeguard any confidential information provided by the DJ hardware partners to Serato. The Commission is unable to require that such arrangements are entered into and would not be privy to the negotiation and enforceability of any such future arrangements.⁴⁵⁷

The SPA does not address our concerns

316. Although ATC submitted that the terms of clause 6 provisions of Schedule 11 of the SPA would "comprehensively address" any risk of ATC using DJ hardware competitors' information,⁴⁵⁸ we are not satisfied that protections designed specifically to safeguard the Sellers' financial interests are sufficient to limit the sharing of competitors' sensitive information between the Parties:

316.1. The relevant provisions do not expressly seek to do that. It would only be by implication that they could be interpreted to have the effect contended by ATC.

316.2. Third-party DJ hardware providers will not have the ability to enforce the clause 6 provisions. Only the Sellers have that ability, and there are likely to be a range of scenarios where it is not in their interests to seek to enforce a breach due to information sharing. Even if they did seek to enforce their

⁴⁵⁴ Email from [].

⁴⁵⁵ Email from [].

⁴⁵⁶ Serato RFI response (20 June 2024).

⁴⁵⁷ ATC has provided the Commission with an early draft of such an agreement proposed to be entered into with []. It is notable that the remedies section of the proposed agreement remains undrafted, and therefore difficult for the Commission to take comfort in the fact of these contemplated future arrangements.

⁴⁵⁸ ATC "Submission by AlphaTheta Corporation on the Statement of Issues" (8 April 2024) at [10.6].

rights, that is most likely to be by way of a retrospective claim for damages which would not prevent the prior use of sensitive information.

316.3. Third party DJ hardware providers will also have no visibility of whether a breach has occurred, or the ability to police information flows between Serato and ATC.

316.4. The obligations under the clause 6 provisions rest on ATC. While ATC's "use" of the information may, according to ATC's submissions, amount to a breach of clause 6, there is nothing in the SPA to preclude Serato from sharing the information with ATC in the first place.

317. While Serato has proposed that there will be a board level protocol which means Serato will be run by a board that is operationally separate from ATC, []]. We are therefore unable to exclude the real chance that certain types of reporting information, or discussions in meeting, would result in ATC gaining the sensitive information of Serato's DJ hardware partners. As noted above, []].

Conclusion on access to sensitive information

318. We are not satisfied that the Proposed Acquisition will not have, or would not be likely to have, the effect of substantially lessening competition in the DJ hardware market due to the merged entity's access to its DJ hardware competitors' sensitive information post-acquisition.

319. We do not consider the proposals from the Parties are sufficient to protect the confidential information that is shared during the integration process and consider that ATC gaining sensitive information of its rivals could lessen competition by providing ATC with a competitive advantage and lessen the incentives on both ATC and its rivals to innovate.

Conclusion

320. The preceding sections have considered the likely unilateral and vertical effects of the acquisition of Serato by ATC. While it is necessary to examine each of these potential effects in turn, the ultimate question we are required to consider is whether we are satisfied that the Proposed Acquisition would not have, or would not be likely to have, the effect of substantially lessening competition in any market.

321. We are not satisfied that the Proposed Acquisition will not have, or would not be likely to have, the effect of substantially lessening competition in the DJ software market due to unilateral effects, and in the DJ hardware market due to vertical effects and the merged entity's access to sensitive information post-acquisition.

322. The Commission is therefore not satisfied that the Proposed Acquisition would not have, or would not be likely to have, the effect of substantially lessening competition in the DJ software and DJ hardware markets in New Zealand.

Determination on notice of clearance

323. The Commission is not satisfied that the acquisition will not have, or would not be likely to have, the effect of substantially lessening competition in a market in New Zealand.
324. Pursuant to section 66(3)(b) of the Commerce Act 1986, the Commerce Commission declines to give clearance to AlphaTheta Corporation to acquire 100% of the shares of Serato Audio Research Limited.

Dated this 17th day of July 2024

Dr John Small
Chair