



ATC / Serato

Serato Submission on Statement of Unresolved Issues

17 June 2024

Consumers within New Zealand

1. The Commission is tasked with promoting competition for the long-term benefit of consumers **within New Zealand**.¹ In New Zealand, in calendar year 2023, those consumers spent a grand total of [] on Serato's DJ software. This can be thought about as roughly a single day's revenue for a single large supermarket. However, unlike spending at the supermarket, expenditure on Serato DJ software is highly discretionary in nature. On any measure, the risk to New Zealand consumers from the proposed transaction is vanishingly small.
2. The Commission's theories of harm as articulated in the SoUI are not really about New Zealand consumers. They are more just a re-statement of various commercial risks perceived to accrue to various multi-national players as a result of the proposed transaction.² Broadly, these parties worry that a preferred commercial partner of theirs (Serato) may treat them differently/unfairly post-transaction. Apart from the fact that the opposite will be true (for reasons that have been explained including in terms of the features built into the SPA but ignored and/or rejected), the reality is that, even assuming the worst of behaviours by the merged entity, all of these parties have the resources and the choices to look after themselves.
3. For example, hardware providers can and do exercise countervailing market power on an ongoing basis in a range of ways, including by:
 - Engineering their own in-house DJ software and promoting it in association with their own hardware;
 - Partnering with other DJ software providers such as Virtual DJ, Algoriddim and Traktor; and
 - developing and promoting a range of devices that bypass Serato DJ software altogether, notably (i) media players with music loaded on to a USB drive and plugged into – Serato DJ software does not include the ability to export music to USB; and (ii) "all-in-one" systems with DJ software embedded.
4. We have provided evidence to show that a full replica of Serato (with a mobile app thrown in for good measure) can be generated from the ground up within a 2-year period.³ Yet the Commission has drawn the opposite conclusion:

¹ Section 1A of the Commerce Act

² As the Commission's own Mergers and Acquisitions Guidelines aptly put it (citing *ANACO Foods Waitara Ltd v AFFCO NZ Ltd* [2006] 3 NZLR 351 (CA), "The substantial lessening of competition test exists to protect the competitive process. It is not focused on protecting individual firms." Commerce Commission, *Mergers and Acquisitions Guidelines* (May 2022) at [2.19].

³ ClearPoint, "DJ Software Build Approach in 2024 – Software Engineering Expert review" (2 April 2024), attached as Appendix E to Serato's submission on the Statement of Issues (8 April 2024). The purpose of

- without even making reference to this evidence (it does not seem to have been considered at all);⁴ and
 - despite being privy to the obvious example of ATC’s own successful development of rekordbox (partly in response to precisely the kinds of concerns raised by opponents around capture by particular providers).
5. To be fair, the Commission has been faced with a sustained opposition to the proposed merger. The motivation for and validity of that opposition insofar as it related to inMusic was discussed in detail in two illuminating submissions made by Eric Gavriluk.⁵ Mr Gavriluk portrays inMusic as being opportunistic – better at buying things than building them. If that is true, maybe their strategic exposure is real. However, it is not the Commission’s job to bail them out.⁶ Regardless though, the merged entity will not be able to assume that inMusic or anyone else will be incapable of their own build. It will remain constrained by the ability of its hardware partners to bypass its products.
 6. Meanwhile, significant upside from the transaction from a New Zealand consumer perspective would be lost if the Commission blocks the merger. Serato was established in a New Zealand garage in 1998. It has grown to be a global business with revenue in the 2023 calendar year of []. If Serato’s commercial projections over the next 5 years are realised (which depends on the concerns identified by the Commission in the SoUI not being realised), the New Zealand founders of the Serato business will receive in excess of [] for the business.
 7. The value that the Serato founders have generated, as recognised in the sale price, is a textbook example of investment in innovation over the longer term being reflected in commercial success. The plan now is to cash out and recycle the capital into “the next thing”. The founders are already actively pursuing other projects with:
 - Steve West building New Zealand EV charging business Charget; and
 - AJ Bertenshaw investing in GoodFor (a New Zealand zero-waste supermarket chain) and Elysian Pharmaceuticals (a New Zealand natural wellness product importer and health clinic).
 8. These are the New Zealand business stories that we need to encourage and foster if we are genuinely interested in the long-term benefit of New Zealand consumers. The Commission blocking the Serato founders’ best path to exit would do the opposite.
 9. Given Serato’s extremely modest commercial footprint in New Zealand, this is not a transaction where an “abundance of caution” approach is justified or appropriate having regard to the high risks for the New Zealand consumer. Given the stakes, this case calls for a robust evaluation of the facts and a commonsense approach.

the ClearPoint report was “to provide a reasonable high level estimate of the software engineering effort to build a competitive product to Serato DJ Pro, Virtual DJ and others”. It concluded that “there does not appear to be any unique or novel constraints to a competitor building a software product to compete with Serato”, and estimated that it would take 12 to 18 months to take a competing product to market (depending on whether the product was built afresh or by an adjacent competitor).

⁴ See discussion in the SoUI at paras [84] to [92]

⁵ Erik Gavriluk, AlphaTheta’s proposed acquisition of Serato (5 April 2024) and Erik Gavriluk, Cross-submission in response to inMusic: Response to InMusic’s cross-submission dated 15 April 2024 (15 May 2024).

⁶ As ATC noted in their submission, inMusic is nearly twice as large a company as ATC – see para 6.12(a) ATC Submission on Sol 9 April 2024

Laptops, phones, CDJs – it's all the same

10. Ultimately, the Commission's entire decision pivots on its reluctance to accept the constraint of mobile apps. There is no need for the conversation to devolve into an esoteric question of market definition within an economist's framework. It is well understood in New Zealand competition law following the *Brambles* decision that market definition merely frames the competition issues. It is not an end in itself. Ultimately, the relevant legal question is one of constraint. In particular, the High Court in *Brambles* found:

It is important to recognise that market definition is a tool for competition analysis rather than an end in itself. A decision to define the market by reference to crates only can provide an appropriate basis for analysis of the competition issues which need to be decided, but defining the market in that way should not lead to any underestimation of the potential substitutability and level of constraint on market participants in that narrowly defined market, from cardboard packaging both pre-merger and post-merger ... the real issue was the degree to which cardboard was recognised as a constraint, whether it was included within the product market or not ... CHEP's primary submission to us was that the Commission had misinterpreted the evidence before it and this had led it to under-estimate the degree of constraint imposed by cardboard. We accept that submission.⁷

11. The Commission has devised theories of harm that make something out of nothing. In particular, the Commission's competition analysis in the SoUI is driven by:

- an artificially narrow approach to market definition that ignores the breadth of options available to DJs; and
- a competition analysis that is static and reflects an antiquated view held within a specific demographic.

12. The Commission finds a "market" unique to DJ software available on laptops, as if somehow laptops are the only way to DJ. The parties have explained numerous times that DJing is ultimately an exercise in playing music to audiences. The truth is that, in terms of equipment, there are myriad ways to DJ, including using:

- Vinyl
- CDJs
- Hardware with embedded DJ software
- Hard drive
- Laptop
- Mobile/tablet.

13. The practical reality is that any DJ can deliver a music set to an audience using any of these options. From an audience perspective, there is no reason to distinguish any of these modes of delivery. Literally no-one goes to a venue to listen to a "laptop DJ". The construct simply does not exist outside of the discourse that has emerged in this regulatory proceeding. It is completely artificial and yet drives all of the concerns set out in the SoUI. In the real world, audiences are wholly indifferent to the mode of delivery that their DJ chooses. They just want to listen to good music.

14. Obviously, different DJs have different preferences about how they might choose to deliver a set. Experienced DJs may well be accustomed to using a laptop. If they have found the DJ software they use with that laptop to be reliable, then they may well choose to continue with that option rather than "churning" to an app based method. That is understandable. However, the fact that there are competitive options that they choose not to take does not mean those options exist in an entirely separate market or that Serato can assume that it is somehow immune to those choices being available. The Commission's entire analysis in the

⁷ *Brambles New Zealand Limited v Commerce Commission* 2003 TCLR 868 (HC), HC AK CIV2115-03 (24 October 2003) at [137].

SoUI is a tautology and if reflected in the Commission's decision will generate a fundamental error.

15. It is trite to say that consumers don't have to exercise a competitive option in order to benefit from it. The availability of a range of different modes of delivery of DJ performance drives Serato to ensure that its product is the best it can be. This is evident from Serato's internal documents that have already been provided.⁸
16. There is no question that laptops, enabled by the emergence of electronically formatted music, have been proven to work well as a tool for DJing. From the early 2000s, laptops emerged as being favoured by a generation of DJs because they were low-cost and high convenience relative to a more traditional vinyl turntable setup. While they met resistance initially as a "fad" by "old school" DJs,⁹ the economics of low-cost/high convenience prevailed over time and the use of laptops became mainstream.
17. That same cycle is being repeated with the emergence of mobile apps. Mobile apps run on a phone and for that reason are:
 - lower cost because the consumer inevitably already has a phone (laptop use is less universal); and
 - more convenient because the phone fits in the pocket of your jeans (a laptop does not). DJs can go out after a gig without having to worry about their laptop.
18. Serato has provided evidence to show that mobile apps are functionally identical to Serato's laptop application.¹⁰ Serato has also pointed that a DJ can perform the same set on their phone or laptop inter-changeably.¹¹ Yet in the SoUI, the Commission has seemingly chosen to dismiss these facts and instead rely on anecdotal feedback regarding existing preferences.¹² The Commission also appears to have overlooked or ignored the evidence that has already been produced that mobile apps are compatible with a range of hardware.
19. The Commission recognises "a degree of substitutability between them for some DJs"¹³ and yet, inexplicably, summarises its view in the SoUI as being that:

*We have not seen strong evidence that mobile apps are likely to impose a material constraint on the merged entity.*¹⁴

20. So, whatever the degree of substitutability (which is acknowledged), the Commission is saying here that mobile apps are literally **irrelevant** from a competition perspective. The extreme nature of this logic can only be explained by the lack of an open mind and in particular an unwillingness to give appropriate weight to evidence provided by the merger parties. Accordingly, we ask that the Commission consider all evidence in a balanced manner.

⁸ For example, see Serato slide pack "Melbourne sessions 2023/2024", including slide 31 stating: Give people a *reason* to use a laptop

⁹ Refer Appendix

¹⁰ NERA, AlphaTheta Corporation/Serato: unilateral effects and foreclosure theories of harm (27 November 2023), at Table 2.4.

¹¹ See, for example, Serato submission in response to Commerce Commission Statement of Issues (8 April 2024) at [26].

¹² For example, SoUI at paras [36], [37.5], [37.6], [41.1], [46], [79.2], [80.1].

¹³ SoUI, para [34]

¹⁴ SoUI, para [51.3]

21. The Commission suggests that Serato's failure to develop a mobile app is consistent with a finding of a separate market for laptop DJ software.¹⁵ However, we have explained that:
- an app is desirable[
]; and¹⁶
 - Serato is at a competitive disadvantage by not having an app but remains competitive by focussing on ensuring the consumer experience on its laptop-based solution is the best it can be.¹⁷

Vertical issues

22. In the SoUI, the Commission remains focussed on the vertical foreclosure theory of harm.
23. The first thing to get clear on is that Serato's path to market is via hardware partners and that any damage to Serato's relationship with any hardware partner inevitably in turn damages Serato's bottom line. It is an obvious commercial "own goal" for Serato to give any hardware partner any motivation to steer their hardware customers away from Serato software.
24. This is precisely why the ring-fencing features in the SPA exist – to confirm that ATC, given its position as a hardware competitor, would not be allowed to intervene to compromise Serato's relationships with its hardware partners and, in doing so, compromise the Serato founders' return on the earnout. As noted in the submission of Serato founder AJ Bertenshaw, this aspect of the SPA was agreed without any pushback from ATC because ATC has never had any intention to do anything other than allow the Serato brand to flourish.
25. The Commission appears to be of the view that the provisions of the SPA must be enforceable by third parties or the Commission for it to be relevant to the Commission's analysis. There is no basis for this in law. The SPA provisions form part of the factual and cannot be ignored.
26. If the Commission truly believes that ATC is buying Serato with a view to tanking the business by forcing Serato to mistreat its commercial partners (notwithstanding ATC having agreed in the SPA not to do this and notwithstanding the overwhelming financial incentive in the form of the earnout for Serato to ensure that ATC makes good on its promise not to do this), then it is difficult to know what can be done to address the Commission's concerns.
27. The Commission's conclusion that ATC has an incentive to engage in vertical foreclosure conduct ignores the significant risks of engaging in such conduct as compared with the modest potential gains. As ATC has submitted, there is no real chance that it would engage in the conduct that the Commission describes in the SoUI, and a finding that it is likely to do so defies commercial commonsense.
28. For the record, regardless of what the Commission (or InMusic) says, this is pie in the sky. It will not happen. It will not happen because:
- ATC has no incentive to do so;
 - Serato will not let it happen because to do so would compromise its earnout, which is the lion's share of its expectations of the purchase price for the Serato business; and
 - the idea that ATC would cash Serato out of its SPA commitments to allow a vertical foreclosure strategy to be pursued is nothing short of a conspiracy theory and in any event is not supported by the numbers, as shown by NERA. The autonomy of the Serato business post transaction was agreed in the SPA before it was even

¹⁵ SoUI, paras [36] and [37.3].

¹⁶ Serato submission in response to Commerce Commission Statement of Issues (8 April 2024) at [48].

¹⁷ Serato submission in response to Commerce Commission Statement of Issues (8 April 2024) at [47] to [51].

understood that competition enforcement agencies might be interested in the transaction. Accordingly, it is reliable evidence of the parties' intentions.

Commercially sensitive information

29. The Commission has queried the hardware protocol and its legal robustness.¹⁸ In doing so, the Commission misses the point – and it all flows from what Serato submits is an absurd view of Serato's market power. Serato has shown that it has not increased its price once since the launch of its subscription price in 2016. In other words, the price has reduced in real terms since that date, even as costs have risen and inflation has taken hold. Only a party with market power could ever contemplate entering into a protocol in bad faith with the intention of changing it or removing it altogether or breaching it and “daring” the hardware partner to seek to enforce the protocol. Notwithstanding the flattering commentary regarding Serato's market position,¹⁹ it simply does not have the luxury of treating its commercial partners with this kind of disdain. Again, this is just not a real world scenario. On the contrary, Serato's growth over many years reflects working tirelessly to engage constructively with all of its hardware partners. Serato has done this because these partners are an **essential channel to market**.
30. The vertically integrated business model is commonplace in competitive markets. Many firms also compete with their suppliers or customers in upstream or downstream markets. Those business recognise the importance of not sharing commercial sensitive information received from a supplier or customer with those parts of the business that compete with that supplier or customer. Information sharing protocols are a common way of recording those arrangements. There is no basis for a theory of harm that vertical integration in this case would be likely to lessen competition in any market.
31. Serato understands and appreciates that hardware partners consider all information shared with Serato to be confidential. That is explicitly recognised in the protocol. The protocol is not designed to be an entrenched legal masterpiece. It is intended to provide commercial comfort to Serato's hardware partners that their confidentiality will be respected post-sale.
32. To be clear, Serato is not saying the information provided by hardware partners is not confidential. Serato of course knows it is and will respect it (regardless of the Commission's apparent sharing of InMusic's belief that it won't). However, if the Commission remains determined to think it is likely that Serato will act (i) in bad faith in relation to the representations made through the hardware protocol and (ii) in a manner contrary to its commercial interests in terms of its ongoing earn-out incentive by betraying the confidence of its commercial partners, then it becomes important (in what Serato considers to be no more than a hypothetical scenario) to focus on the nature of the information shared and the question of whether the confidential information shared is materially sensitive **from a competition perspective**.
33. It remains Serato's position that, for any hardware partner such as InMusic who, like the Commission, is concerned that Serato will act in bad faith in breach of the protocol and contrary to its own commercial interests:
- the only information that hardware partner **needs** to share that could reasonably be considered to be sensitive from a competition perspective is the prototype; and
 - even still, the reality is that the market operates so that nobody copies a prototype without first seeing how it performs in the market – this is because no-one knows whether a new idea is going to gain traction in the market.

¹⁸ SoUI at [156]-[160].

¹⁹ For example, SoUI at [110] and [138.2].

34. So, even if we assume that Serato will act in a way that will not happen, there would be no adverse impact on competition.

35. The evidence provided by ATC to the Commission (not mentioned in the SoUI) that it has [

] shows that these issues are routinely managed in these markets.²⁰ This evidence shows that the Commission's concerns as articulated in the SoUI are overstated.

A note on switching

36. In the SoUI, the Commission finds high switching costs for consumers of Serato software.²¹ No facts are cited to support this finding and Serato is not aware of any facts that could support this finding. From Serato's perspective, switching is practically seamless given that rival software automatically reads Serato's library. The only cost for a subscriber would be any additional costs associated with higher prices charged by rival software providers.

²⁰ Meeting with NZCC on 29 April 2024.

²¹ SoUI, para [90]

APPENDIX

<https://alimaclean.com/2008/05/08/djs-and-turntablism-are-hipsters-and-laptops-killing-the-art-form/>

<https://gearspace.com/board/electronic-music-instruments-and-electronic-music-production/329299-what-djs-use-only-laptops-live.html>

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Lives for gear
BLACK AGENT
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Exactly, using a laptop isn't DJing.

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DJ's using laptops

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I don't mind laptops so long as it brings something new to the sound and the DJ's still jump around and get excited. I'll always prefer CD's/vinyl as it seems to involve more live skill, rather than having things pre set. But then when you hear Sasha's... **See more**

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Jim Holloway
To be honest, I still know people who consider CD's to be cheating. But I think you're right - if the end result is loads of people dancing, it shouldn't matter. I've been using CD's more and more lately as I love using the loop facilities. It has no... **See more**

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