

inMusic’s Response to Serato Audio Research Limited’s Submission in Support of AlphaTheta Corporation’s Clearance Application to Acquire Serato

I. Executive Summary

- a. inMusic Brands, Inc. and its subsidiaries and affiliates including inMusic New Zealand Limited (inMusic) submit this response to Serato Audio Research Limited’s (Serato) Submission to the New Zealand Commerce Commission (Commission) on 9 November 2023 in respect of the acquisition by AlphaTheta Corporation (ATC) of Serato.
- b. ATC never expected to apply to the Commission for clearance. Although Overseas Investment Office (OIO) approval was required by law due to the size of the transaction, Commission approval was not, and therefore, ATC chose to ignore the Commission even though the acquisition clearly raises anti-competition concerns. ATC thought it could slip the transaction past the Commission and did not foresee that Commission approval would be required.¹
- c. This explains why—apparently believing that closing was inevitable—ATC’s initial public statements², and Serato’s communications with inMusic shortly after the deal was announced³ are entirely inconsistent with statements and assertions subsequently made in the Application and in Serato’s Submission as the parties belatedly engaged with the Commission.
- d. As a result of unexpectedly having to explain why the deal should be allowed, ATC’s eventual filing of the Application presented a conundrum: how to defend the indefensible. ATC’s market dominance in DJ hardware and its co-dominance with Serato with respect to DJ software made the proposed acquisition clearly untenable. Therefore, ATC opted to mislead and speculate baselessly about the future while offering little to no compelling evidence to support its position. Serato’s Submission

¹ inMusic recently obtained communications through an Official Information Act request that show ATC was attempting to convince the OIO to allow the transaction to complete unconditionally. Fortunately, the OIO held firm and conditioned approval on Commission clearance/non-intervention. It was only then that ATC and Serato amended their Stock Purchase Agreement to condition closing on Commission clearance, and ATC agreed to submit the Application.

² inMusic will not repeat the arguments made in its original Submission, but rather will refer to ATC’s press releases and internal investor communications as described in inMusic’s Submission.

³ As previously recounted to the Commission by inMusic, when inMusic raised concerns about the confidentiality of its business information with Serato, Serato’s first reaction was to tell inMusic that it could not ensure that inMusic’s Confidential Information would be protected. Serato then asked if, in light of this, it should stop development on existing products and return inMusic’s Confidential Information. Serato also pressed inMusic to sign a “Change in Control” letter. Under the terms of the licence agreement between inMusic and Serato, either party was required to obtain the consent of the other party before the agreement could be assigned. For purposes of the agreement, a change in control constitutes an assignment. inMusic presumes that all other Serato hardware partners were presented the same document and signed it. inMusic has refused to be coerced into such consent but understands why other hardware providers may have been left with no choice but to sign given that independent hardware manufacturers depend so substantially on Serato.

continues the façade.⁴ Notwithstanding that Serato’s Submission, which inMusic reasonably assumes (like the ATC Clearance application) was coordinated with ATC, self-servingly advances ATC’s disingenuous narrative, it is also self-defeating: Serato’s arguments and purported evidence largely support inMusic’s position, not ATC’s and Serato’s.

II. MIDI Mapping

- a. Serato contends at the outset that vertical foreclosure is impossible because any DJ hardware can be used with any DJ software. Not so. inMusic submits that, after its demonstration to the Commission and subsequent interview on 9 November 2023, it should be clear that “MIDI mapping” a controller to DJ software, while *technically* “possible,” is extraordinarily challenging, has many limitations and cannot be accomplished by most end users. Specifically, the Commission may recall from the in-person demo that the motorized platters on inMusic’s RANE controller have over 3,000 reference points on the platters that must be read by optical couplers. To maintain proper sync between the platter movement and the audio track in the DJ software, those couplers must be precisely integrated with the DJ software. This is not a simple MIDI-mapping procedure. It is a painstaking process that requires substantial effort over many months and only Serato’s software performs particularly well due to the deep collaboration between inMusic and Serato.⁵
- b. ATC’s and Serato’s continued insistence that the availability of MIDI mapping prevents them from foreclosing hardware competitors is easily their most cunning distortion. While not outright false, the claim is superficial; ATC and Serato vastly oversimplify the process and ignore that almost no one does it because it is complicated, and end users just want their products to work out of the box. In short, the Commission should reject the claim that MIDI mapping prevents foreclosure because it rarely happens in practice, and nor would it happen post transaction so as to constrain a combined ATC/Serato.
- c. Moreover, the claim is especially peculiar coming from Serato because Serato DJ software is the most challenging to map. Serato’s own website notes that, “Hardware features that **cannot** be remapped at this stage are the Jogwheels/Platters, Input Switches, Shift buttons and Performance Pad Mode buttons.”⁶, all of which are major components that are not optional for a performing DJ. While noting (at [2]) that “any hardware” (emphasis added) can be mapped, Serato then inserts the massive caveat that a Serato supported soundcard must be available. Indeed, such a soundcard is not

⁴ Although it is notable that Serato has dropped the pretense that this deal is “primarily” about Serato’s music production software.

⁵ In fact, ATC’s signature controller with motorized platters, the DDJ-REV7, only works with Serato software and not ATC’s own rekordbox, presumably because Serato excels at motorized platter integration and ATC has been unable to match it.

⁶ <https://support.serato.com/hc/en-us/articles/209377487-MIDI-mapping-with-Serato-DJ-Pro>. (Emphasis added.)

an off-the-shelf product that can be installed and used by an end user. Only an official Serato certified accessory has a Serato supported soundcard. In other words, if the hardware is already compatible with Serato, it can be mapped to Serato (with exceptions as noted above)⁷, but most users would simply opt to use the plug-and-play compatibility in that circumstance and not perform manual mapping.

- d. Stepping back, Serato is claiming that rather than switching to ATC (the undisputed largest hardware provider with a strong and powerful brand, which also offers Serato), customers would instead attempt an extensive, highly technical and likely fruitless MIDI mapping exercise, which by Serato’s own admission cannot be achieved for core components such as the platters, in an attempt to somehow achieve compatibility with the very software which they can use if they switched to ATC hardware.

III. Vertical Foreclosure

- a. Serato is wrong about vertical foreclosure on both the facts and the law. Serato contends that a foreclosure theory is not supportable because Serato has neither market power nor incentive to foreclose competition. But the test is not whether Serato existing on its own as it does today has the power and incentive to foreclose. It is whether a combined ATC and Serato have the power and incentive to foreclose. The answer is an indisputable yes.
- b. ATC will face very different incentives as owner of Serato than Serato faces today. ATC is constrained today in both the DJ hardware market and DJ software market by the presence of Serato. ATC must offer Serato (but not necessarily other DJ software) with its DJ hardware because enough hardware customers prefer Serato over rekordbox that ATC would lose hardware sales if it did not offer Serato. ATC also must continue to develop rekordbox so that it does not fall behind its only real DJ software competitor in Serato. If rekordbox were considered by the market as less-featured than Serato, ATC could lose both software sales and hardware sales if customers believe that a combination of, for example, Serato and RANE had a richer feature set than rekordbox and ATC hardware. Serato is similarly constrained today by the presence of rekordbox. If Serato did not keep up with feature development against rekordbox, users could migrate to rekordbox. Additionally, partnering with many DJ hardware providers gives Serato the best chance to compete with rekordbox by offering substantial consumer choice.

⁷ See also <https://djtechtools.com/2018/04/11/hacking-serato-djs-midi-mapping-jogwheels-touchstrips-and-modifiers/> for an excellent description of the challenges and limitations of trying to MIDI map Serato: “Serato has been relatively secretive about the MIDI implementation of their software. Though the software allows the use of any MIDI device, **many features are only available on certified controllers. You can’t map your own jogwheels, functions like needle search / slicer are restricted, and there are no shift control layers or modifiers to create advanced mappings.**” (Emphasis added).

- c. Post-acquisition, ATC will have very different incentives: it will want to capture as many hardware customers (and the associated margin) as possible. Since it will then have the majority of DJ software market share between rekordbox and Serato, ATC's options for doing so will be endless. For example, for users who prefer Serato, foreclosing inMusic would force consumers into ATC hardware. ATC could also turn Serato into a different product, such as entry-level only or cater to a specific type of DJ, to differentiate it from rekordbox, or simply achieve that status over time by focusing development efforts on rekordbox. In this scenario, ATC could continue to collect Serato revenue but minimize competition for rekordbox and foreclose inMusic from competing at the high-end where some of inMusic's most-acclaimed controllers (e.g. the RANE Four) compete. Regardless of what ATC chooses, there is no escaping that ATC and Serato will no longer operate as a constraint on each other, and ATC will have many anti-competitive options to maximize revenue and/or decrease costs at its disposal.

IV. Market Power

- a. Again, the operative issue is not Serato's market power and incentives as they stand today; it is whether the combination of ATC and Serato would have market power and the incentives to harm competition/increase prices post-acquisition. ATC already has substantial market power, and post-acquisition, ATC will have even more substantial market power. Even if, however, the Commission were to consider whether Serato presently has market power, the answer is still yes.
- b. Serato contends that it is not an "important input" or "must have." In support, Serato notes that it does not yet have an app, nor has it secured music streaming integration from major music digital service providers such as Spotify, Apple and Amazon.⁸ Serato further suggests that there are many alternative offerings to Serato and provides seven examples of high-profile DJs using certain of these alternatives. Of course, it does not mention that the key competitive constraint it current faces is the presence of rekordbox.
- c. Serato's claims would be laughable if this were not such a serious matter. inMusic reminds the Commission yet again that ATC has agreed to pay over NZD 100 million for Serato—a company that earned only a quarter of that much in revenue last year and approximately 10% of that number in EBITDA. It is an unserious argument by both ATC and Serato to pretend that ATC will not benefit significantly from purchasing its only real software competitor. ATC knows that Serato lacking an app and Amazon music streaming integration has not held back Serato in any way, which is why ATC agreed to pay the purchase price it did. As we stated at the outset of this response, ATC never expected to apply for clearance. Arguments suggesting that

⁸ Serato's claim is slightly misleading. No DJ software has Spotify or Apple integration. Also, there are many other streaming services including Tidal, Beatsource, Beatport and SoundCloud, all of which Serato has. The only streaming service that inMusic has secured but Serato has not is Amazon. Otherwise, Serato has integrated the same streaming services as every other DJ software and is not at a commercial disadvantage.

Serato is not the market leader for DJ software are concocted merely for the benefit of the Application.

- d. Turning to the specific examples Serato cites in support of its claim that it does not have market power:
 - i. The substantial redactions in Serato’s Submission show just how much confidential and commercially sensitive information Serato possesses relative to the rest of the industry. As the only DJ software provider that collects licence fees (and therefore receives product plans and strategies) from effectively 100% of the DJ hardware industry, Serato is **uniquely** positioned **to obtain, analyze and leverage** the most important competitive intelligence relating to consumer use of DJ hardware. If this acquisition were allowed, all that data will be owned by ATC.⁹ Notably, Serato has made clear that it fully intends to provide customer data to ATC post-acquisition.¹⁰
 - ii. Following ATC’s lead, Serato also attempts to distort reality and have the Commission believe there are many competitive alternatives by pointing to anecdotal evidence of a few famous DJs using software and equipment other than Serato and/or ATC. Serato’s dominance, however, is self-evident: ATC (like inMusic and others) pays Serato (and not any other DJ software provider) millions of dollars in licence fees per year, and ATC has agreed to pay over NZD 100 million to acquire Serato. This is because there are hundreds of thousands of Serato users, and it is the top choice, together with ATC’s rekordbox. That Serato has managed to find seven very isolated instances of DJs using non-Serato/ATC products does not change the fact that the vast majority of DJs choose to use Serato and/or ATC. But even if these few instances were relevant, Serato’s examples are not supportive of their claim for the following reasons:

⁹ It is notable that, despite the different opinions and arguments concerning the facts and law among those who have submitted to the Commission concerning this acquisition, the one fact that no one disagrees with is that ATC is far and away the dominant DJ hardware provider, owning a substantial majority of the market. Placing vast amounts of customer data in ATC’s hands will be ripe for exploitation and likely increase its already overwhelming market share.

¹⁰ See Serato Hardware Partner Confidentiality Protocol at Section 5, explaining that Serato views customer data as outside the definition of “Confidential Information” in its licence agreement with inMusic, and Serato therefore contends it is legally permitted to share such customer data, which includes analytics regarding the usage of partner hardware, with ATC.

1. [redacted].¹¹ [redacted].¹² [redacted].¹³
2. Serato’s reference to Laidback Luke similarly fails when additional context is considered. [redacted].¹⁴ [redacted].¹⁵ [redacted].¹⁶
3. With respect to DJ JFB, while it is true that inMusic retained him to perform for a promo for our Denon DJ SC6000M launch, he is nevertheless a dedicated Serato user. In fact, Serato neglects to inform the Commission that JFB is one of their featured “Artists” with an entire page dedicated to him on the Serato website.¹⁷ Just seven weeks ago, JFB posted an Instagram video wherein he uses Serato and Pioneer DJ, and he tagged both.¹⁸ The fact that Serato suggests that one of its own high-profile Artists uses “alternative” DJ software is simply incredible and again proves the point that one-off and occasional sets on other DJ software and/or equipment do not change the fact that most DJs use Serato and/or rekordbox most of the time.
4. Invisibl Skratch Piklz is, in fact, a group of DJs, which at times has included Serato Artists D-Styles and Mix Master Mike.¹⁹ As with JFB, although there is a video of the group using Algoriddim, a recent video on Instagram plainly shows them DJing with laptops.²⁰ We also note that Invisibl Skratch Piklz appears to have a commercial relationship with Algoriddim.²¹
5. DJ Duo KIREEK are precisely the type of users that inMusic mentioned in its original submission. They have been using

¹¹ [redacted].

¹² A “rider” is commonly used by performers to inform the venue of specific items required for their performance.

<https://pytch.co.uk/knowledge/what-is-a-rider#:~:text=A%20rider%20is%20a%20document,A%20rider%20states%20these%20requirements>.

inMusic had found little traction with convincing venues to install its equipment on their own because the venues believed that performers would not want to use inMusic equipment. By paying major DJs to include Denon DJ equipment in their riders, inMusic believed it would force venues to purchase their equipment and then DJs would use the equipment, like it and purchase it. Despite inMusic’s DJ hardware earning rave reviews, some of which Serato cited (see the Submission at [18]), the campaign was largely a failure, proving again that ATC cannot be displaced, irrespective of inMusic selling compelling products at attractive price points and marketed by top DJs.

¹³ [redacted].

¹⁴ Brand Ambassador Personal Services Agreement, as amended, between inMusic and Laidback Luke, attached.

¹⁵ <https://www.youtube.com/watch?v=-TxgiTyw9zw>.

¹⁶ [redacted].

¹⁷ <https://serato.com/artists/jfb>.

¹⁸ https://www.instagram.com/reel/Cxpv1nEoSSp/?utm_source=ig_web_copy_link&igshid=ODhhZWM5NmIwOQ=

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¹⁹ <https://serato.com/artists>.

²⁰ <https://www.instagram.com/p/Ctpx82qp00t/>. It is difficult to tell, but it looks like they are using Serato.

²¹ https://www.stokyoworld.com/products/dj-q-bert-x-shortkut-x-d-styles-isp-fugitives-of-funk-djay-pro-ai-control-vinyl-white-12-single?fbclid=IwAR3tBsr3ibIdrPau07zARoAIImQRRFoQkElr80-Z_cSn1IUxot7vQ_dlf2hY.

Traktor for many years.²² As the Commission may recall, prior to rekordbox, the top two DJ software options were Traktor and Serato. rekordbox has eclipsed Traktor for many reasons, but Traktor remains viable precisely because of users like KIREEK who cannot imagine using anything else.

6. In sum, inMusic has never contended that every DJ, in every situation, uses only Serato or rekordbox. Many high-profile DJs experiment with alternative DJ software for many reasons, including due to paid sponsorships deals. ATC/Serato presenting random clips of certain DJs using DJ software other than Serato or rekordbox (some from 6 years ago) does not change the fact that the overwhelming majority of professional DJs primarily use Serato or rekordbox over other DJ software, especially in live settings when reliability matters the most.

V. Exclusivity

- a. Although most of the section is redacted, to the extent inMusic can ascertain Serato's argument, it appears that Serato contends that it is simply one DJ software option to be used with DJ hardware. Again, Serato focuses on the minor exceptions and not the rule.
- b. Of course inMusic would like to reduce its dependence on Serato and has therefore experimented, as Serato points out, with promoting its own Engine DJ software over Serato in a few instances, typically with little success. Serato, however, neglects a few key facts. As the Commission can see from inMusic's response to its RFI, the overwhelming majority of inMusic products are licensed with Serato. Prime 4, Party Mix II and Party Mix Live are all products that are branded with Serato, and inMusic pays a licence fee to Serato for every unit sold, regardless of whether the user ever activates their Serato account. No other DJ software is promoted on those products or their packaging. Serato cites inMusic's product websites where we do, in fact, show that such products are "compatible with" other DJ software. As explained previously, all compatibility work for non-Serato software is done by the software provider. It simply makes good business sense that after, for example, Virtual DJ has done the compatibility work, that inMusic would promote that compatibility if there is a chance it could increase sales.²³
- c. Serato is also correct that embedded systems have received positive reviews from industry commentators.²⁴ However, neither inMusic's promotional activities nor positive reviews have increased its hardware market share against ATC or diminished

²² <https://blog.native-instruments.com/traktor-20-japan/>.

²³ Notably, even a sale of inMusic hardware to a Virtual DJ customer who never uses Serato would bear a royalty from inMusic to Serato.

²⁴ Submission at [18].

in any way Serato’s dominance in the DJ software market. This is also supported by the fact that ATC only licences Serato in addition to its own rekordbox. Neither inMusic nor ATC can afford to stop paying Serato licence fees because Serato is ultimately what the customers want.

VI. Opportunities from the Proposed Transaction

- a. In three short paragraphs (only two of which inMusic can see), Serato baldly dismisses, without support, the idea that ATC would foreclose competition. At [26], Serato glibly states that foreclosure would be “irrational” because ATC would lose revenue from Serato hardware fees and subscription revenue. But Serato ignores that:
 - i. the likely alternative for a lost Serato customer is rekordbox, not any of the lower-tier competitors; and
 - ii. as the Commission is aware, such is the importance of Serato to consumers that ATC itself ensures full compatibility with Serato, which means that ATC will maintain the Serato subscription revenue with the only difference being that customers will now use Pioneer, not e.g. inMusic, hardware.
- b. Of course, ATC would also benefit from the increased profit from increased hardware sales and the wider (substantial) strategic benefit from competitively marginalizing its only real hardware competitor.
- c. In fact, not only does inMusic believe ATC will use Serato to harm its hardware competitors who rely on Serato, it has concerns as to whether Serato will remain in its current form. Keeping Serato separate and business “as is” means operating a second office, maintaining a separate codebase and employing duplicative developers. On the other hand, collapsing Serato into ATC will save ATC substantial costs and hasten payback of its \$100 million. The far likelier scenario from a commercial standpoint is for ATC to eliminate Serato and incorporate its best features into rekordbox.
- d. Serato further imagines—again without explanation—that “bringing together” Serato and ATC will somehow enhance competition. Serato’s claim is almost too absurd to rebut. Given the enormous market share that ATC would enjoy, its most logical business decision would be to increase prices and slow innovation. Without an independent Serato to constrain ATC, it will be free to operate in anti-competitive ways. Software innovation will slow and software prices rise. Hardware innovation will slow and hardware prices rise. ATC will have no incentive not to, other than pure benevolence. In inMusic’s experience—and presumably the Commission’s as well—large, multinational, public companies do not voluntarily act benevolently.

VII. Conclusion

- a. Serato’s Submission adds nothing of substance to the Commission’s consideration of ATC’s Application. Filled instead with anecdotal evidence, groundless speculation,

misguided predictions and misleading narratives, the Commission should afford it no weight. Serato merely repeats and amplifies the same failed arguments that ATC advances. For the many reasons inMusic has presented, there is no basis for the Commission to be satisfied an SLC is not likely. Accordingly, the Commission should decline to give clearance to the Application.