

27118834000

IN THE COMPETITION TRIBUNAL OF SOUTH AFRICA

CASE NO:

In the matter between:

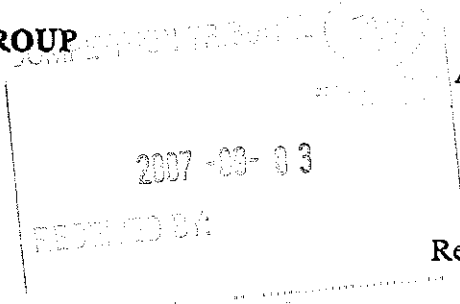
**REPLICATION TECHNOLOGY GROUP
(PROPRIETARY) LIMITED**

Applicant

and

GALLO AFRICA LIMITED

Respondent



FILING SHEET

BE PLEASED TO TAKE NOTICE THAT the Applicant hereby files a Notice of Motion before the Competition Tribunal.

DATED at SANDTON on this **31** day of AUGUST 2007.

DENEYS REITZ ATTORNEYS
Applicant's Attorneys
82 Maude Street
SANDTON
2146
Tel: (011) 685-8500
Fax: (011) 883-4000
Ref: 22/REP/62 - Mr P C Viljoen

And to: **GALLO AFRICA LIMITED**
First Respondent
Johncom House
4 Bierman Avenue
Rosebank
JOHANNSBURG

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Received copy hereof on this ___ day
of AUGUST 2007.

For: GALLO AFRICA LIMITED

And to: **THE COMPETITION COMMISSION**
3rd Floor, Mulayo,
The DTI Campus,
77 Meintjies Street
Sunnyside
PRETORIA

Received copy hereof on this ___ day
of AUGUST 2007.

**For: COMPETITION
COMMISSION**

And To: **THE COMPETITION TRIBUNAL**
3rd Floor, Mulayo,
The DTI Campus,
77 Meintjies Street
Sunnyside
PRETORIA

Received copy hereof on this ___ day
of AUGUST 2007.

For: COMPETITION TRIBUNAL

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**BEFORE THE COMPETITION TRIBUNAL OF SOUTH AFRICA
REPUBLIC OF SOUTH AFRICA**

CASE NO:

In the matter between:

**REPLICATION TECHNOLOGY GROUP
(PROPRIETARY) LIMITED**

Applicant

and

GALLO AFRICA LIMITED

Respondent

NOTICE OF MOTION

KINDLY TAKE NOTICE that the applicant intends making application to the above Competition Tribunal at 10h00 (or so soon thereafter as Counsel for the applicant may be heard) on a date to be arranged by the Registrar of the above Honourable Tribunal for an order in the following terms:

1. That the respondents be and are interdicted and restrained from enforcing clause 13 of the Sale Agreement (a copy of which is annexed hereto and marked X) and/or from requiring that the applicant abide by the aforesaid clause 13 and/or from implementing such clause on the basis that such clause constitutes a restrictive and/or prohibited horizontal practice as contemplated in section 4(1)(b) of Act No. 89 of 1998.
2. That the relief sought in paragraph 1 above operates and/or remains in force until the earlier of -
 - 2.1 a final determination of the applicant's complaint in terms of Act No. 89 of 1998 (and which complaint will be lodged with the Competition Commission

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simultaneously herewith) that clauses 2.9 and 13 of the aforesaid Sale Agreement constitute restrictive and/or prohibited practices as contemplated in terms of section 4(1)(a) alternatively section 4(1)(b) and section 5(1) of Act No. 89 of 1998; or

- 2.2 a date that is 6 (six) months after the date of the granting of the relief sought in paragraph 1 above.
3. That the costs of this application be paid by the respondent in the event of it opposing this application.
4. Granting the applicant such further and/or alternative relief as the Honourable Tribunal deems fit.

KINDLY TAKE NOTICE that the accompanying affidavit of **SHIMON HENRY TEPERSON** with its annexures and the supporting affidavit of **MERVYN SHEIN** will be used in support of this application.

TAKE NOTICE FURTHER that if you intend opposing this application, you are required to:

- (a) Notify the applicant's attorneys (being **DENEYS REITZ ATTORNEYS** of 82 Maude Street, Sandton, 2146, telefax number 011-883-4000 and Ref: 22/REP/62 – Mr P C Viljoen) within 5 (five) days of receipt hereof of your intention to oppose; and
- (b) To file your answering affidavit, if any, and to serve same on the applicant's attorney within 15 (fifteen) days of being served with this Notice of Motion at the address and/or telefax number set out above.

27118834000

DATED at SANDTON on this 31 day of AUGUST 2007.

[Signature]

DENEYS REITZ ATTORNEYS
 Applicant's Attorneys
 82 Maude Street
 SANDTON
 2146
 Tel: (011) 685-8500
 Fax: (011) 883-4000
 Ref: 22/REP/62 - Mr P C Viljoen

To: **THE REGISTRAR**
THE COMPETITION TRIBUNAL
 3rd Floor, Mulayo,
 The DTI Campus,
 77 Meintjies Street
 Sunnyside
 PRETORIA

Received copy hereof on this ___ day
 of AUGUST 2007.

 For: COMPETITION TRIBUNAL

And to: **GALLO AFRICA LIMITED**
 First Respondent
 Johncom House
 4 Bierman Avenue
 Rosebank
 JOHANNESBURG

Received copy hereof on this ___ day
 of AUGUST 2007.

 For: GALLO AFRICA LIMITED

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And to: **THE REGISTRAR**
THE COMPETITION COMMISSION
3rd Floor, Mulayo,
The DTI Campus,
77 Meintjies Street
Sunnyside
PRETORIA

Received copy hereof on this ___ day
of AUGUST 2007.

For: COMPETITION
COMMISSION

27118834000



competition tribunal south africa

Notice of Motion

Date: _____ File # _____

To: The registrar of the Competition Tribunal

Concerning the matter between:

REPLICATION TECHNOLOGY GROUP (PTY) LTD (Applicant)

and GALLO AFRICA LIMITED (Respondent)

Take notice that the APPLICANT
intends to apply to the Tribunal for the following order:

That the Respondent be and is interdicted and restrained from enforcing clause 13 of the Sale Agreement (which is annexed hereto marked "X") and/or from requiring that the Applicant abides by the aforesaid clause 13 and for from implementing such clause on the basis that such clause constitutes a restrictive and/or prohibited practice as contemplated in Section 4(1)(b) of Act No 89 of 1998

Name and Title of person authorised to sign:

Peter Campbell Vijoen

Authorised Signature:

Date:

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**BEFORE THE COMPETITION TRIBUNAL OF SOUTH AFRICA
REPUBLIC OF SOUTH AFRICA**

CASE NO:

In the matter between:

REPLICATION TECHNOLOGY GROUP (PTY) LTD

Applicant

and

GALLO AFRICA LIMITED

Respondent

FOUNDING AFFIDAVIT

I, the undersigned,

SHIMON HENRY TEPERSON

do hereby state and declare under oath as follows:

THE DEPONENT

1. I am an adult male and the applicant's Chief Executive Officer.
2. I am duly authorised to bring this application on behalf of the applicant, to depose to this affidavit, represent it in this application and do all things necessary in connection therewith. Proof of my authority is evidenced by annexure "A" hereto.
3. The allegations contained in this affidavit, unless otherwise indicated by the context, fall within my personal knowledge and are, to the best of my knowledge and belief, both true and correct.



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4. Where I make submissions of a legal nature in this affidavit, I do so on the advice of the applicant's legal representatives.
5. I have approximately 26 years' of experience within the analogue music manufacturing and replication industry. More recently, I have 11 years of uninterrupted experience within the compact disc (CD) manufacturing, replication and packaging industry and 6 years' of similar experience within the digital versatile disc (DVD) industry. In light of this experience, I believe that I have the necessary expertise, and am suitably placed, to express the opinions that I do in this affidavit regarding, *inter alia*, the relevant markets, their participants and their respective market shares.

THE PARTIES

6. The applicant is **REPLICATION TECHNOLOGY GROUP (PTY) LTD.**
 - 6.1 The applicant is a private company with limited liability duly registered and incorporated as such in accordance with the Company Laws of the Republic of South Africa.
 - 6.2 The applicant's principal place of business is RTG House, 18 Sixth Street, Wynberg, Johannesburg.
 - 6.3 The applicant is the "Seller" as defined in the Sale Agreement annexed to the Notice of Motion and marked "X" ("*the Sale Agreement*"). This application pertains specifically to the enforceability of clause 13 of the Sale Agreement.
7. The respondent is **GALLO AFRICA LIMITED.**
 - 7.1 The respondent is a public company with limited liability duly registered and incorporated as such in accordance with the Company Laws of the Republic of South Africa.



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- 7.2 Its principal place of business, and its chosen *domicilium citandi et excutandi* in terms of the sale agreement, is at Johncom House, 4 Biermann Avenue, Rosebank, Johannesburg.
- 7.3 The respondent is the "*Purchaser*" as defined in the Sale Agreement.
- 7.4 For ease of reference, the respondent and its associated group of companies will simply be referred to hereinafter as "*Gallo*" unless otherwise specified.

INTRODUCTION

8. I depose to this affidavit in support of an application for interim relief in terms of section 49C of the Competition Act, No 89 of 1998 ("*the Act*").
9. The applicant seeks an order interdicting and restraining Gallo on an interim basis, from enforcing clause 13 of the Sale Agreement.
10. Clause 13 of the Sale Agreement constitutes market division by allocating customers, as is prohibited by section 4(1)(b)(ii) of the Act. Clause 13 can be found at pages 12 and 13 of the Sale Agreement. For ease of reference, clause 13 is restated in paragraph 31 below. Clause 13 will hereinafter simply be referred to as the "*offending clause*".
11. The offending clause imposes a restraint of trade obligation on the applicant. The offending clause operates in favour of Gallo.
12. The offending clause prohibits the applicant from furnishing CD and DVD manufacturing, replicating, DVD authoring¹, editing, printing, packaging, marketing and sales services to approximately 592 specified customers ("*the prohibited customers*" or "*the prescribed customers*") in the South African manufacturing industry. These services will hereinafter collectively be referred to as the "*prohibited services*".

¹ This is the process of creating a DVD video that can be played on a DVD player.



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13. The prohibited services are the "*prescribed services*" as defined in clause 2.3.7 of the Sale Agreement (page 4) as read with the definition of "*specified business*" in clause 2.3.14 of the Sale Agreement (page 5).
14. The "*prescribed customers*" are defined in the Sale Agreement as being any person who is a customer of Compact Disc Technologies (Pty) Limited ("*CDT*") and as listed in annexure "B" to the Sale Agreement. These are the prohibited customers referred to in this application.
15. The prohibited customers constitute, at least, approximately 80% of all the customers within the relevant market (the relevant market is dealt with below). Each of the prohibited customers is independently listed in Annexure "B" to the Sale Agreement.
16. The interim relief is sought pending the final determination of a complaint by the applicant to the Competition Commission. The complaint will be that clause 13 (the offending clause) of the Sale Agreement constitutes a restrictive and/or prohibited practice. It is the applicant's contention that the offending clause contravenes sections 4(1)(a), 4(1)(b)(ii) and 5(1) of the Act. The complaint will be lodged simultaneously with, or very shortly after, the launching of this application.
17. The continued survival of the applicant (and competition within the market) is intrinsically tied up to the granting of the interim relief. Should the applicant cease to trade, effective competition within the market will be eliminated. Absolute control over the markets will be left in the hands of two entities: Sonopress and Gallo,² albeit that Sonopress is not a proactive participant in the market. This accordingly means that the market and its customers will be left at the mercy of Gallo.

THE RELEVANT MARKET

18. The market in issue is the composite CD and DVD manufacturing, replicating, DVD authoring, editing, printing, packaging, marketing and sales market in the context of the music and film (movie) home entertainment industry ("*the market*").

² There are other competitors within the relevant market. They however account, at best, for only approximately 4% of the total market revenue. These participants do not have the infrastructure, expertise, capacity or ability to fill the void which the demise of the applicant would create within the market.

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19. Simply put, CDs and DVDs are optical discs used to store digital (media) data. DVD's, however, allow for approximately 8 times the data storage capacity (single-layer, single-sided) of a CD.
20. Although CDs and DVDs products are household commodities sold every day across the world (in 2004, the annual worldwide sales of CD audio, CD-ROM discs reached approximately 30 billion units), the optical disc replication market is highly specialised, highly technical and both capital and machinery intensive. The market is not, in any sense, a normal manufacturing market. In this regard, I refer to copies of pages from Frontiers website (www.frontierdvd.co.za)³. The web pages indicate that entailed in the CD and DVD replication process (annexure "B1"); that entailed in the CD and DVD printing process (annexure "B2") and in the DVD authoring process (annexure "B3"). As set out below, the barriers to entry to the market are exceptionally high.
21. The market is in turn divided into two sub-markets: the CD market and the DVD market. Whilst not important for purposes of this application, these two sub-markets are in turn divided into further sub-markets. The sub-markets within the CD market include the CD-Rom and CD music markets. The DVD market comprises of, *inter alia*, the DVD movie market and the DVD music market.
22. Internationally, the market is controlled by a few large international concerns. They are Technicolor, Cinran and the Sonopress Group.
23. For the reasons set out below, locally the market is controlled by Gallo. It holds market power. Sonopress South Africa (Pty) Ltd ("*Sonopress*") and the applicant are the only other principal participants in the market, due to, *inter alia*, the high barriers to entry. During the financial year to 30 June 2007, the total sales revenue of the three participants within the markets was estimated at approximately R285 million.
24. The customers in the market (*i.e.* the customers for the services) are divided into two content groups: major content holders and minor content holders.

³ Frontier is dealt with below under the topic "*Relevant background / the dramatis persona*".



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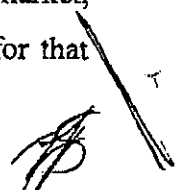
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- 24.1 Major movie content holders are characterised by the fact that they have both international and local studios and artists within their respective content stables. Major movie DVD content holders include Nu Metro Home Entertainment, a part of the Johnnic Communications group of companies ("*Johncom*" and of whom Gallo forms part) and Ster Kinekor Home Entertainment ("*Ster Kinekor*"). Between them, Nu Metro and Ster Kinekor hold, *inter alia*, the licences in South Africa to all the content of the Hollywood Studios, major international movie content and substantial local movie content.
- 24.2 Minor movie content holders only represent smaller international studios. That said, there are minor content holders, such as New Heights (Pty) Limited and Next Video (Pty) Limited, who are substantial minor movie content holders.
- 24.3 Major Music Content Holders concern themselves with international music content and local Afrikaans and Black music rights.
- 24.4 Minor Music Content Holders might have one or two international acts but are principally dependent on local music content.
25. This application pertains to the contractual restraint precluding the applicant from providing the prohibited services to the market. Were it not for the offending clause, the applicant would be participating in the market and furnishing the prohibited services.
26. The (content) customers generally perceived to be the biggest in the market, both in terms of volume and revenue, are:
- 26.1 Sony BMG;
- 26.2 EMI;
- 26.3 Universal;
- 26.4 Ster Kinekor;
- 

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- 26.5 Nu Metro; and
- 26.6 Gallo Record Company.
27. The market for dealing with the larger more sought after (content) customers is inherently more lucrative. The demand by these clients for manufacturing and replication is constant and largely predictable. The timing for movie (big screen) DVD release dates is predictable, uniform and pre-determinable. Accordingly, it is easier to anticipate and cater for the demands and seasonal needs of these customers. The "runs" for these customers are usually longer and greater in volume (units). The units generally have a higher unit price.
28. From a mere glance at the list of prohibited customers, it is self apparent that Gallo contractually enjoys the exclusive custom of all of the larger sought after clients (other than Sony BMG).
29. The barriers to entry into the market are, as already indicated, exceptionally high.
- 29.1 A new participant entering into the market today and wishing to participate at an international standard and quality, would need to invest, at least, approximately R30 million upfront. This would simply entitle such new participant to the running of a single DVD line (at a start-up cost of €1 million). An additional €1.5 million would be spent on mastering equipment. The printing and packaging equipment required by this new participant would additionally cost approximately €300 000.00.
- 29.2 The lead time for such new participant to be up and running would be at least 3 to 4 months. The lead time is of course dependent on the new participant having the required intellectual and technical capital. There is a massive skills shortage in respect of the personnel required and necessary to run the machinery required for the manufacturing and replication of a CD / DVD line, as well as the necessary mastering (moulding) equipment. The necessary individual would need as a minimum the necessary NI1 or NT2 background. Additionally they would require 3 training rotations of 6 months each (this is the training afforded to the applicant's employees).
- 29.3 For the reasons set out below, should the applicant be compelled to vacate the market, the resulting vacuum would not be readily filled up by a new participant (or for that



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matter the existing participants, including the smaller participants, other than Gallo. Sonopress, as indicated above, is not a pro-active participant in the market. It already has a dedicated work allocation. It has historically shown no interest in expanding upon same. Even should it now show such interest, it does not have the capacity to do so. The balance of the participants in the market (other than Gallo) is small and diverse. They hold neither the capital nor the technical know how to increase market share; notwithstanding the vacuum which would be created by the applicant's departure.

- 29.4 In any event, I sincerely believe that Gallo would act swiftly and decisively. It has the means to neutralise any participant from obtaining the (vacated) market share given up by the applicant. It has the financial muscle and market power to do so.

THE OFFENDING CLAUSE

30. Prior to restating the offending clause, the following definitions at clause 3.2, (page 4 onwards) of the Sale Agreement must be listed:
- 30.1 "*the / this agreement*" means the Sale Agreement together with its schedules and annexures;
- 30.2 "*CDT*" means Compact Disc Technologies (Pty) Limited registered under the registration number 1990/000268/07 according to the laws in force in the Republic of South Africa (*i e.* CDT);
- 30.3 "*competing services*" means any services which are the same as, or similar to, or complete with any prescribed services;
- 30.4 "*effective date*" shall mean 31 July 2006;
- 30.5 "*prescribed customer*" means any person who is a customer of CDT as listed in Annexure "B" to the Sale Agreement; and
- 30.6 "*prescribed services*" means any service rendered by CDT in the ordinary course of business and relating to the specified business.



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30.7 "specified business" means the business conducted by CDT of the manufacturing and sale of CDs and DVDs and matters incidental thereto.

31. The offending clause provides as follows:

"13 RESTRAINT"

13.1 *Subject to the Purchaser acquiring not less than the total number of sale shares in terms of this agreement, the Seller undertakes to the Purchaser that for a period of 24 (twenty four) months after the effective date, it will not, without the prior written consent of the Purchaser, render any competing services to such prescribed customer.*

13.2 *The area of restraint referred to in clause 13.1 shall be the Republic of South Africa.*

13.3 *The restrained party acknowledges –*

13.3.1 *that the Seller would not have entered into the purchase of the sale shares and the sale claims unless the restrained party had agreed to the restraint contained in the clause;*

13.3.2 *that the restraint is the minimum restraint required by the seller to provide protection against unfair competition and that in the circumstances it is fair and reasonable, and necessary for the protection of the interests of the Seller that the restrained party should be restrained in the manner set out in this clause.*

13.3.3 *Each and every restraint contained in this clause 13 is separate and divisible from every other restraint in the clause and from any other restraint so that if any one of the restraints is or becomes unenforceable for any reason, that restraint will be severable and will not effect the validity of any other restraint contained in this clause or otherwise.*

13.3.4 *The restraints contained in this clause will be capable of being enforced by the Seller or its assigns or any of its shareholders from time to time. However, they will cease to be enforceable should CDT be placed in final liquidation unless such liquidation results from a restructuring of CDT.*




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13.4 *It is specifically recorded and agreed, for the sake of clarity, that, notwithstanding anything to the contrary contained herein,-*

13.4.1 *should any prescribed customer wish to obtain any competing services from the Seller or a third party, the Seller shall be entitled to provide the competing services to such prescribed customer subject to agreement being reached between the Seller and Purchaser on a form of compensation for the duration of this restraint, and the Seller shall not be in breach of any provision contained in the clause 13, and*

13.4.2 *the provisions contained in clause 13.4.1 shall in no way entitle the Seller to approach or solicit any prescribed customer in order to provide the competing service."*

32. The condition referred to in 13.1 of the offending clause was met. The respondent (purchaser) acquired the shares in question on 31 July 2006.
33. Accordingly, the offending clause is presently of full force and effect and the applicant is bound by same and competition within the market is artificially constrained by same.
34. The offending clause divides up and allocates the customers in the market by prohibiting the applicant from dealing with the prohibited customers. These specified customers include the largest (in revenue and volume) and most influential customers within the market. This anti-competitive arrangement and the clear restriction on supply to the market exist solely as a result of the offending clause.
35. The offending clause imposes no reciprocal restraint obligation on Gallo. Gallo is not burdened by any similar obligation in the nature of a restraint or limitation on its ability or entitlement to conduct business – whether as to area, customers, products, suppliers, services or otherwise.
36. I additionally do not believe that the offending clause protects any protectable proprietary interest held by Gallo. I am advised that the offending clause can be appropriately regarded as a "naked" restraint of trade.
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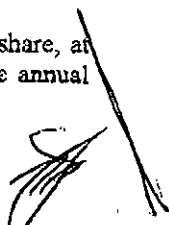
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RELEVANT BACKGROUND / THE *DRAMATIS PERSONAE*

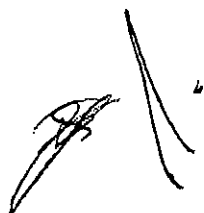
37. In order to facilitate a proper appreciation of this application and the need for the interim relief, regard must be had to the key participants in the markets and the relevant background to this application.
38. At present, there are effectively three principal competitors in market.⁴ They are:
- 38.1 The *applicant*. It was formed during 2000.
- 38.1.1 At the time of its creation, the applicant acquired the underlying analogue manufacturing and replication business of Abacus Technology Holdings.
- 38.1.2 At the time, management held 50.1% of the shares in the applicant. RMB Corvest ("*Corvest*") held the other 49.9% shareholding. Corvest is a private equity company and forms part of the FirstRand group.
- 38.1.3 The applicant participates in the market subject to the operation of the restraint in respect of the prescribed services.
- 38.1.4 The applicant is the only truly independent principal competitor within the market.
- 38.1.5 During the period 2005 to 30 June 2007, the applicant participated in the markets via its wholly owned subsidiary Frontier DVD (Proprietary) Limited ("*Frontier*"). On 30 June 2007, the business of Frontier was collapsed back into the applicant for tax purposes. Frontier is presently an empty shell. (The applicant's website is still to be updated in this regard).
- 38.1.6 The applicant's present manufacturing facility comprises 2 DVD lines and 1 CD line.
- 38.1.7 The two DVD lines are presently running at 40% of their maximum capacity. The CD line is running at between 25% and 30% of its maximum capacity.

⁴ I say "*effectively*" because, as already indicated, while there are other participants, they are small and share, at best, a total aggregate of only of 4% of the optical disc replication market with an estimated aggregate annual turnover of R10 million.



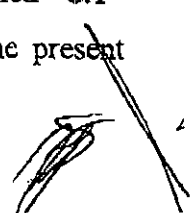
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- 38.1.8 The applicant's turnover was approximately R57 million for the financial year ending June 2007. It has a market share of 20%.
- 38.1.9 The applicant has approximately 90 (ninety) employees of which 90% are previously disadvantaged individuals.
- 38.1.10 I mention that whilst the applicant also participates in the market for the manufacture of analogue formats (e.g VHS and audio cassettes), this is a rapidly declining market which is in the process of being replaced by the market. The revenue from this market is not included in the applicant's abovementioned turnover.
- 38.2 Within Gallo is CDT. As far as I have been able to establish, CDT is a wholly owned subsidiary of the respondent. The respondent is in turn, I believe, owned a 100% by Johncom.
- 38.2.1 Gallo is the leading participant in the market in Africa. Its manufacturing facility comprises 8 CD lines and 4 DVD lines.
- 38.2.2 For the year ending 31 March 2006, 32 (thirty two) million units were produced by Gallo. It has an estimated annual turnover of R177 million. It holds approximately 62% of the combined CD and DVD market.
- 38.2.3 Gallo is the dominant participant in the market and holds market power. It has the financial backing of the Johncom Group.
- 38.2.4 Historically, Gallo runs its operations within the market at an annual capacity of approximately 75%. During high demand periods (such as, *inter alia*, the last quarter of the year, the Easter and July periods) this moves to 100% (*i.e.* full capacity).
- 38.3 *Sonopress* is a wholly owned subsidiary of Arvato Storage Media GMBH Germany ("*Arvato*").
- 38.4
- 38.4.1 Arvato is in turn owned by Bertelsmann AG also of Germany.
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- 38.4.2 Bertelsmann is the owner of BMG (Bertelsmann Music Group).
- 38.4.3 The Sonopress Group website records that Bertelsmann employs approximately 76,000 people (2003) and has annual revenues of €17 Billion (2003).
- 38.4.4 Arvato has sixteen facilities (subsidiaries) worldwide. It has facilities in, *inter alia*, Australia, Brazil, England, France, Germany, Hong Kong, Ireland, Mexico, Philippines, South Africa, Spain, and USA. It is present on every populated continent.
- 38.4.5 Sonopress' South African facility comprises three CD lines and two DVD lines.
- 38.4.6 It has an estimated annual turnover of R40 million and a combined DVD and CD market share of approximately 14 %.
- 38.4.7 Sonopress is not an active market increasing participant in the market. In this sense, Sonopress does not actively go out and market itself and neither does it actively seek an increased market share. It has historically shown itself to be content with only fulfilling the manufacturing, replication, *etc.* requirements of Sony BMG.
- 38.4.8 That said, Sonopress' focus is principally on the CD portion of the market. In respect of the DVD portion of the market, it only holds approximately 1 to 2%.
- 38.4.9 Its core (and to all intents and purposes) sole customer is Sony BMG. In fact, there have been occasions where Sonopress has simply been unable to handle the demands of Sony BMG and has sought to engage Gallo in sharing its load in this regard.
39. As indicated above within Gallo is the respondent and, to the best of the applicant's knowledge, the respondent is the 100% shareholder of CDT. Again, to the best of the applicant's knowledge **Johncom** is the holding company (100% shareholder) of the respondent.
- 39.1 A copy of an organogram for the Johncom Group is annexed hereto and marked "C.1" and "C.2". It was obtained from the Johncom website. It indicates the present
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Johncom group structure and the Johncom group structure post 1 October 2007. If the applicant is wrong in its understanding of the Johncom Group and Gallo the respondent is hereby invited to set out the correct position. Once this information is furnished, the applicant will ask for leave, if necessary, to supplement this affidavit in this regard.

39.2 Whilst there can be no doubt that Gallo is a competitor of the applicant, the respondent is also a competitor of the applicant. As much, was unequivocally acknowledged by the respondent in a letter addressed by their legal representatives on 4 May 2007 to the applicant's then attorneys. At paragraph 2.3.4 of the letter, the respondent's attorney's state:

"Upon receipt of the up front pro-rata payment, both our client [i.e. the respondent] and RTG [the applicant] would be able to tender for the requirements of Ster Kinekor and Next Video".

A copy of the letter is annexure "F.14" hereto. This letter is placed in its proper context later on in this affidavit.

39.3 Additionally and notwithstanding the above, the applicant believes that for purposes of this application, Gallo can and should be regarded as a single economic entity.

39.4 I say so for the following reasons:

39.4.1 CDT is not a party to the sale agreement yet it is a direct beneficiary of same. The prohibited customers listed in Schedule B to the sale agreement are a mere recordal of CDT's customer list as at the date of the sale agreement.

39.4.2 The respondent controls the fate of CDT. The respondent is the sole shareholder of CDT. The respondent appoints and controls the board of directors of CDT. The respondent and Gallo additionally have common directors [as is apparent from the attached copies of extracts of the records of the Companies Office (annexure "D1" and "D2")].

39.4.3 On a proper construction and interpretation of the Sale Agreement and the offending clause, the offending clause was clearly inserted by the respondent in



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order to protect the interests of Gallo generally and CDI specifically (and accordingly the respondent's investment interest in CDT). I mention that the offending clause was foisted upon by the applicant in the circumstances set out below.

39.4.4 Additionally, the organogram sketch of the present structure of Johncom (annexure "C" hereto) records CDT as part and parcel of the Gallo Group and the music and manufacturing arm of Johncom. There are accordingly common structural links between the respondents and between the respondents and Johncom.

39.4.5 Johncom includes the results of Gallo in its financial reports [see annexure "E.1" to "E.5" hereto being extracts of the "reviewed interim results for the 6 months ended 30 September 2006" for Johncom (the complete results have not been annexed hereto for purposes of avoiding prolixity)]. Of particular importance is the following statement contained in the extracts:

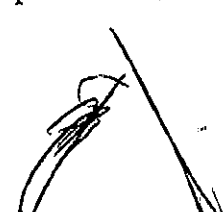
"Effective 31 July 2006 Johncom acquired the minority 40% of Compact Disc Technologies (CDT), giving it full ownership of Africa's largest CD and DVD manufacturing plant".

40. In order to understand how the three key participants (Gallo, Sonopress and the applicant) came to hold their respective shares in the market, a brief history of the South African optical disc replication market is set out.

40.1 Prior to the introduction of the CD format internationally and locally (the latter in the early to mid 1980's), vinyl was the format of choice. There were two vinyl (record) manufacturing companies in South Africa: Gallo and EMI.

40.2 The introduction of the CD format internationally and locally led, initially gradually and then rapidly, to the decline of the vinyl format.

40.3 In due course and during approximately 1993/1994, EMI closed their vinyl record manufacturer. Gallo was left as the only vinyl record manufacturer and replicator and enjoyed a monopoly over the vinyl market.



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- 40.4 However and during approximately February 1991, the key players in the South African music content industry, namely Gallo, EMI and Warner Music (trading as Tusk Music) formed a joint venture. The purpose of the joint venture was to set up and operate the first CD manufacturing plant in South Africa (incidentally also the first on the African continent). Prior to this, all CD's were imported.
- 40.5 The joint venture was an *en commandite* partnership in which the disclosed or *commanditarian* partner was CDT (*i.e.* the corporate vehicle through which the manufacturing would take place). Accordingly, CDT acquired and owned the manufacturing plant. CDT set about manufacturing CDs and in due course DVDs for its then-undisclosed joint venture partners.
- 40.6 CDT quickly became very profitable. This was solely as a result of the collusive and monopolistic environment in which it traded. It was the sole manufacturer and replicator of CDs, and in due course DVDs, in South Africa.
- 40.7 During the early 1990's and given, *inter alia*, the political change in South African and the maturing (local) market, the international "*record*" companies decided to establish themselves directly in South Africa. This and other factors led to a market re-organisation.
- 40.7.1 Gallo, whilst losing its content licences, acquired the rights to the Warner licence for, to the best of my knowledge, 10 (ten) years. As indicated below, this relationship was further cemented in due course.
- 40.7.2 During 1996, EMI parted ways with the joint venture and set up its own CD manufacturing plant; manufacturing for itself.
- 40.7.3 Shortly thereafter, during 1997, BMG obtained access to essentially its own dedicated CD manufacturing plant (*i.e.* Sonopress and which formed part of the Bertelsmann group of companies).
- 40.7.4 CDT became a wholly owned subsidiary of the respondent. At first, the business of CDT was incorporated into the respondent. The business of CDT was then



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sold to a shelf company and in which the applicant acquired approximately 28%. In terms of an option, the applicant acquired in due course, a further approximately 12% of the shareholding in CDT.


40.7.5 During approximately 2002, Gallo negotiated with Warner to enter into a 50/50 joint venture. Today, Warner Music Gallo Africa (WMGA) is a music based content joint venture between Warner Music International and Johnnic Communications. WMGA houses the worldwide digital rights to Gallo's entire domestic catalogue.

40.7.6 During 2002/2003 Sony and BMG negotiated a joint venture internationally (Sony BMG). The local effect of this joint venture was that Sony was subsumed, in South Africa, into the business of BMG and become known as Sony BMG Music South Africa ("Sony BMG"). I understand that this transaction was only approved by the competition authorities in 2005.

40.7.7 When all was said and done, the market re-organisation left Gallo, EMI and Sonopress as the only effective participants in the market. As EMI manufactured for itself (i.e. its own content) and Sonopress primarily for Sony BMG, Gallo was the only entity of any consequence servicing the needs of the balance of the market.

40.8 Having lost its monopoly and dominance over the market, and its customers, and despite having turned to an export DVD market, Gallo's financial prospects in the market looked bleak from approximately 1996 onwards. Pursuant to the implementation of a turnaround strategy, Gallo approached the applicant for assistance. Gallo realised that whilst the applicant participated principally in the analogue products market (VHS and audio) should the applicant enter the market (the applicant had shown a cursory interest at the time), this would have serious consequences for Gallo within the market and handicap Gallo's turnaround strategy.

40.9 Accordingly and on 7 December 2001, an agreement was concluded between the applicant and the respondent, represented by Johncom, and in terms of which the applicant acquired, for a purchase price of R8 million, 100% of the respondent's



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analogue business (and in so doing the respondent disposed of its interest in a rapidly outdated analogue business to the applicant).

- 40.10 On 13 March 2002, the respondent sold 28.55% of its shareholding in CDT to the applicant. In due course, the applicant acquired a further approximately 12% in CDT in terms of an option. This left the applicant with 40% of the shareholding in CDT.
- 40.11 During approximately 2002, EMI elected to withdraw from the manufacturing market. EMI internationally had commenced a cost cutting exercise and had closed down its manufacturing and replication plants worldwide almost overnight. The applicant was asked to take over EMI's manufacturing and replication obligations and plant. However, given the applicant's then-relationship with Gallo, the applicant was unable to entertain EMI's offer. Instead, the applicant arranged for EMI's facilities to be taken over by Gallo. (I point out that no money changed hands in this transaction.) EMI then appointed Gallo as EMI's exclusive manufacturer of CD's and DVD's (again no money changed hands). (I also point out that prior to this EMI was not a customer of Gallo.) (At that point in time Sony was still a client of CDT, see 40.7.6 above)
- 40.12 Accordingly, eventually, the key participants in the market were reduced to two: Gallo (*via* CDT) and Sonopress. Again, however, only Gallo was engaged in meeting the demands of the balance of available market (*i.e.* the market less Sony BMG).
- 40.13 During approximately March 2003 and in terms of the shareholders agreement, I was appointed as the CEO of CDT. I was immediately charged with turning around and growing Gallo's (CDT's) financial prospects in the market. I remained in this position until July 2006.
- 40.14 The applicant however had its own problems. The analogue market continued to decline rapidly. In an act of desperation and survival and during 2004, the applicant permitted Johncom to acquire the applicant's CD duplication division for an amount of R8 million. This cash inflow permitted the applicant to settle its most pressing debts. The applicant up to this stage had effectively survived on the repayment of shareholders loans and, in due course, on the dividends received from its shareholding in CDT. The




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applicant increasingly began to rely on loans from its shareholders. The applicant's participation in the analogue market was no longer capable of sustaining the applicant.

- 40.15 In a further attempt to address its financial predicament and during July 2005, the applicant successfully approached Gallo for purposes of purchasing a DVD line and mastering machine in order for the applicant to participate in the adult entertainment market (Gallo was not in this market and had shown no interest in this market).
- 40.16 This additional financial respite for the applicant was only temporary. A change in the Johncom management structure, and accordingly its financial policy, directly impacted on the applicant's financial position. Gallo, at the instance of Johncom, reconsidered and altered CDT's dividend policy during approximately March 2006. This had a direct and immediate impact on the applicant's dividend income. Johncom and Gallo were at all times intimately aware of the applicant's need for dividend payments. They knew that the applicant's financial survival depended on dividend payments. The applicant's repeated pleas in this regard, made by myself, fell on deaf ears. The financial predicament imposed on the applicant by the alteration of CDT's dividend policy required that the applicant obtain additional financial assistance. In this regard, it raised R2 million in terms of further overdraft facilities. The facilities were obtained from First National Bank.
- 40.17 The applicant's financial position worsened. The applicant's majority shareholder, Corvest, who at this time held a shareholding in the applicant of 67% (the balance of the shares were held by management), increasingly pushed the applicant for a return on its investment in the applicant.
- 40.18 Accordingly, the applicant approached Gallo to either (a) purchase the respondent's 60% shareholding in CDT or (b) permit the applicant to increase its shareholding in CDT to 50%. Gallo rejected both proposals.
- 40.19 The applicant's 40% interest in CDT (pursuant to a right of first refusal contained in Shareholders Agreement⁵) was then offered to the respondent (the draft agreement

⁵ If required, a copy of the Shareholders Agreement will be made available. It has not been attached to this affidavit in order to avoid prolixity. The respondent (as well as CDT) should be in possession of the agreement.




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being prepared by Corvest).⁶ This offer was similarly refused by Gallo.

- 40.20 Corvest then informed the respondent that it would purchase the 40% shareholding. The respondent was unhappy with Corvest, effectively a bank, as its shareholder (despite it being for all intents and purposes a "sleeping" partner). The respondent refused to consent to the sale to Corvest and instead acquired the applicant's 40% interest in CDT in terms of the Sale Agreement (incorporating the offending clause). In due course and after having received payment of its portion of the purchase price in terms of the Sale Agreement, Corvest ceased to be a shareholder of the applicant. With the benefit of hindsight, it appears that Corvest was actively seeking to exit its shareholding in the applicant. The only way it could do so was by requiring the applicant to sell its shares in CDT and subsequently repay its loans. These funds would then be used by Corvest to exit as a shareholder.
- 40.21 The ownership of the applicant now rests entirely in the hands of the applicant's management.
- 40.22 (In the interim, Gallo's position in the market had gone from strength to strength due to the applicant's involvement and management as well as the monopolistic and competition free environment in which it operated and held sway.)
- 40.23 The offending clause was incorporated at the insistence of Gallo.
- 40.23.1 Given the fact that the driving personalities behind both the respondent and CDT were Prakash Desai and Hermanus (Herman) Trollip, sight cannot be lost of the benefits obtained by Gallo from the offending clause.
- 40.23.2 Given the applicant's increasingly constrained financial position, the applicant had simply no option but to succumb to Gallo's demand in this regard. There was no negotiation. The applicant's hands were tied and it was presented with a *fait accompli vis-à-vis* the offending clause.

⁶ I mention that First National Bank, the applicant's bankers at the time, had indicated to the applicant that it would only consider renewing the facilities granted to the applicant on the sale by the applicant of its 40% shareholding




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- 40.23.3 The applicant was placed under additional pressure by Corvest, its majority shareholder, to finalise the agreement. Corvest merely wished to recover its portion of the purchase price as quickly as possible (prior to divesting from the applicant).
- 40.23.4 The list of the prohibited customers was arrived at simply by taking the active contents of CDT's debtors' book as at the date of the Sale Agreement.
- 40.24 I point out that at no time did the applicant contemplate, let alone appreciate, that the offending clause constituted a prohibited practice in terms of the Act. Had the applicant known at the time of the competition law implications of the offending clause, the applicant would not have consented to the Sale Agreement. In fact, the applicant only found out recently of the competition law implications of the offending clause. The applicant does not want to be a party to a prohibited practice.
- 40.25 I pause to mention that should the respondent and/or Gallo restructure, for example, if they merge with any other customer or supplier in the market, the restraint nevertheless continues irrespective of how non-competitive or manipulative such restructuring may be to the market.
41. Pursuant to the conclusion of the Sale Agreement, the applicant acquired a CD line and another DVD line and commenced marketing its products and services (identical to those of CDT) to a diminished and ring-fenced portion of the market.

THE STATUS QUO

42. The applicant is in dire financial straits. In order to break even the applicant requires a net annual turnover of R64 million at 50% gross (together with interest and depreciation). For the 12 (twelve) month period ending June 2007 (*i.e* since the commencement of the operation of the offending clause) the applicant suffered a loss of R12 million (approximately a R1 million a month).
43. This substantial loss was made notwithstanding the fact that that a sizeable portion of the purchase price paid to the applicant in terms of the Sale Agreement (and which accrued to the
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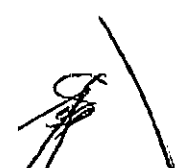
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applicant's management shareholders as opposed to the applicant's former bank / private equity shareholder) was directly reinvested in the applicant by its management. Had this not been done, the applicant would in all likelihood already have ceased to exist.

44. This loss is additionally having a direct impact on the ability of the applicant to service its debt obligations. If this loss is not arrested as a matter of some urgency, the applicant will simply have to close its doors. The applicant is unable to carry this loss for the remainder of the restraint period. Accordingly, the effluxion of the restraint by time will have no impact whatsoever on the financial predicament of the applicant.
45. The applicant's share of the purchase price for CDT received from Gallo was R15 million. This amount was immediately reinvested into the business of the applicant. This investment was made primarily so as to allow the applicant to participate in the market (albeit in the curtailed market). The offending clause has impacted severely on the business of the applicant to the extent that the losses incurred thus far have far exceeded any benefits received by the applicant in respect of the purchase price.
46. The applicant is ready, willing and able to service the customers whom it is restrained from dealing with. In fact, certain of those customers have indicated to the applicant that they are unhappy with service delivery and pricing of Gallo.

EVIDENCE OF THE RESTRICTIVE PROHIBITED PRACTICES

47. I refer to that set out above in respect of the offending clause and its impact on the market.
48. I believe that Gallo's dominance and market power in the market is entrenched by the offending clause. Gallo enjoys access to all of the market and control over approximately 62% of this market.
49. As Sonopress effectively only services the interests of Sony BMG, the balance of the market is shared between the applicant and the respondent. However, the respondent is handicapped by being compelled to operate under a restraint.
50. There are no (effective and independent) competitors to Gallo within the market.




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THE APPLICANT'S DAMAGES


51. Should the interim relief not be granted, the applicant will suffer serious and irreparable damage. The applicant will cease to exist.
52. Customers on the restrained list have regularly approached the applicant to fulfil their orders since approximately July 2006. The respondent has threatened to interdict the applicant if it transacts business with these customers. A copy of the respondent's correspondence in this regard, is attached marked Annexure "F.7".
53. The applicant's plant has the capacity to enter into the restrained portion of the market, but is unable to do so solely because of the offending clause. At present, the applicant's plant is grossly underutilised. It is currently engaged at well below 50% of its maximum capacity.
54. To date, the capital investment in the applicant totals approximately R40 million. This is comprised of mastering equipment, one CD Line, two DVD Lines, two offset printing machines and packaging equipment. At the risk of being redundant, this capital investment will obviously be lost should the operation of the offending clause not be interdicted.
55. The 90 (ninety) employees of the applicant and, accordingly, their families, will suffer in as much as the applicant may be compelled to engage in retrenchments or, worse still, to close its business completely.

ABSENCE OF ALTERNATIVE REMEDY

56. There is simply no adequate alternative remedy available to the applicant.
 57. The applicant has attempted to engage the respondent in terms of clause 13.4 of the offending clause. In this regard, I refer to the attached correspondence between the parties and their legal representatives, a bundle as annexure "F". The correspondence confirms Gallo's obdurate and *mala fide* attitude and the manifestly unreasonable and overbearing terms it seeks to impose on the applicant prior to Gallo's limited relaxation of the terms of the offending clause.
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58. In an attempt to limit the impact of the offending clause on the business of the applicant, the applicant engaged during May 2007 a deputy CEO and a Chief Financial Officer. It was hoped that his financial expertise would assist the applicant in dealing with the severe financial consequences of the offending clause. The first step taken pursuant to the appointment was to restructure the applicant and its subsidiary, Frontier. The financial reporting structure of the applicant was restructured and the applicant was organised into divisions. The accounting software across the group was rationalised and the costing systems were revised. Continuing internal steps were engaged to lessen the impact of the offending clause. That said, the applicant is nevertheless now in a position where should the operation of the offending clause not be suspended, the applicant will have to close its doors.
59. Should the accompanying complaint about the offending clause simply be investigated in due course, the aforementioned anti-competitive harm would continue to contaminate the market until such time as any proceedings were brought by the commission and ultimately determined. I am advised that this process (including possible reviews and appeals) could take an indefinite amount of time, but at the very least a year.
60. The applicant simply does not have the luxury of time. The applicant is ready willing and able to, *inter alia*, immediately enter into the restrained portion of the market and deal with the prohibited, presently restrained, customers.
61. In any event, I am advised that there simply are no alternative remedies available in terms of the Act which would remedy the anti-competitive affects of the offending clauses (even on a forward looking basis).
62. Furthermore and as already indicated, the applicant is reluctant to continue to be a party to a prohibited practice. Should interim relief not be granted and in the light of section 65(1) of the Act, the applicant and the respondent, will be required to continue to be parties to a prohibited practice in terms of the Act.
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BALANCE OF CONVENIENCE

63. The balance of convenience, with respect, overwhelmingly favours the granting of interim relief.
64. At present, and in fact for approximately the last year, Gallo has enjoyed, and still enjoys, market power over, and an effective monopoly in, the market and absolute power over the prohibited customers.
65. The granting of the interim relief will lessen Gallo's stranglehold and monopoly over the market and allow the applicant to enter into and compete in the restrained portions of the market and in so doing offer a competitive alternative supplier to all of the market.
66. However, and as already indicated, the applicant simply cannot wait for relief in the ordinary course (*i.e.* the final determination of its complaint in terms of the Act). Should the interim relief not be granted, the applicant will be required to close its doors and the final determination of the applicant's complaint will, for all intents and purposes, become academic. The applicant will, in the interim, have been precluded from being able to supply the prohibited customers in the market and Gallo's monopoly and dominance over this market will have been entrenched and advanced.
67. The closure of the applicant's business will result in a loss of a R40m (forty million rand) investment and the jobs of the 90 (ninety) people employed in the applicant's business..
68. The only inconvenience that the respondent will suffer as a result of the granting of interim relief, is, it is submitted, the inconvenience suffered by any competitor in an open and unrestrained market. In this particular instance, it will merely be the inconvenience of a new competitor entering into a domain controlled by Gallo and the accompanying loosening of Gallo's stranglehold.
69. In the short term, Gallo should only lose a relatively small portion of an extremely large market share (it is in any event due to lose the benefit of the restraint during July 2008). Such loss will only be in circumstances which, nevertheless, allow Gallo to continue marketing to




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its entire market, so that there is no "loss" as such, but merely an opening of the door to competition.

70. It would, with respect, be somewhat misplaced and opportunistic for Gallo to proffer the aforesaid inconvenience (and possible prejudice) as a reason why interim relief should not be granted. Any goodwill that Gallo may have developed in relation to the prohibited customers was conceived solely in an artificially sanitised, anti-competitive and protected environment and in breach of the provisions of the Act.
71. In any event, I am advised and believe that given the applicant's inherently reasonable prospects of success in respect of the complaint against, *inter alia*, the offending clause, the balance of convenience for the granting of the interim relief must, with respect (and to the extent it remains relevant), weigh heavily in favour of the applicant.
72. Notwithstanding the above, the continued operation of the offending clause has the direct consequence of an ongoing breach of an express provision of the Act by Gallo and the applicant.
73. Gallo has abused its dominant position by ensuring that the prohibited customers do not approach the applicant. Even in circumstances where Gallo is unable to satisfy the needs and demands of such customers. In this regard, I specifically refer to Ster Kinekor and Next Video.
74. Few customers are in a position to disregard Gallo's whims solely due to the dominance which it enjoys in the market. Accordingly, not only are customers reluctant to commit themselves to paper in this application, set out their complaints to Gallo's dominance and the impact of the restraint, they are also reluctant to deal with the applicant in an environment where their sole source of service is Gallo.

THE NEED FOR THIS RELIEF

75. I refer to that set out above regarding the inherent need for the granting of the relief. Not only is the applicant's continued survival dependent on the granting of the relief, but the consequences for the market, should the relief not be granted, would be dire. Competition
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within the market would effectively be excluded. Gallo's hold and control over the market would be absolute.

76. The applicant simply cannot wait for the investigation by the Competition Commission to take place in the ordinary course without the necessary interim relief.
77. This application has been prepared as expeditiously as possible. Whilst the applicant was alive to the financial consequences of the offending clause, it simply had no input in respect of its imposition on the applicant. That said, the applicant had no option but to attempt to ride out the storm (*i.e.* the period of the restraint). It however quickly became apparent to the applicant that it would simply be unable to do so.
78. The applicant then began to look to the agreement itself for appropriate relief. In this regard, an approach was made to Gallo during the middle of December 2006. In this regard, I refer to annexure "F.1". The respondent's dilatory conduct is self-evident from annexures "F.2" to "F.5". Pursuant thereto, there was an attempt by the applicant to engage Gallo in terms of clause 13.4 of the sale agreement. This attempt ran aground during May 2007 and pursuant to the wholly unreasonable demands of Gallo.

This application has been brought as expeditiously as possible.

79. At no time, prior to mid August 2007, was the applicant alive to, or advised of, the Competition Law aspects of the Sale Agreement (and the offending clause) despite being represented by its previous attorneys (and consulting with an eminent senior counsel). It was only as a result of a representative of the applicant serendipitously learning of the existence of the *Nedschroef* judgment of the Competition Tribunal⁷ on the internet that the applicant learnt of the possible Competition Law implications of the offending clause. The judgment in turn led the applicant to the applicant's present attorneys of record and the launching of this application.

⁷ *Nedschroef Johannesburg (Pty) Limited and Teamcor Limited and three others* (Case no 954/TR/Oct 05)



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CONCLUSION

80. In the light of the above and whilst I am advised that interim relief is not readily granted, the applicant's continued existence is intimately and inherently dependant on the granting of the interim relief sought.
81. Similarly, the potential for removing the respondent's anti-competitive control over the fundamental customer market is intimately and inherently dependant on the granting of interim relief. Without the applicant, there is simply no real competition in the market place.
82. Not only does the applicant require the assistance and protection of the interim relief but so does the market.
83. Accordingly, I believe that a suitable case is made out for the granting of the interim relief sought by the applicant in its Notice of Motion.
84. In respect of the issue of costs, costs will only be sought against the respondent should it oppose this application. Absent opposition, costs should be in the cause of the final proceedings.



SHIMON TEPERSON

I hereby certify that the deponent declares that the deponent knows and understands the contents of this affidavit and that it is to the best of the deponent's knowledge both true and correct. This affidavit was signed and sworn to before me at _____ on this _____ day of AUGUST 2007 and that the Regulations contained in Government Notice R1258 of 21 July 1972, as amended, have been complied with.



COMMISSIONER OF OATHS

Full Names:

Business Address:

Designation:

Area/Office:

hendrik johan strydom
 commissioner of oaths
 ENS forensics RSA
 150 west street sandown
 sandton 2196

