



*CORPCAPITAL*  
Investments

## J. HAMBURGER: STATEMENT

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**J. HAMBURGER STATEMENT**

**1 OCTOBER 2003**

**EXECUTIVE SUMMARY AND  
INTRODUCTION TO THE STATEMENT OF  
JADE HAMBURGER**

1.10.2003

- 1 I am a qualified chartered accountant. Prior to joining Corpcapital in 1998 I had both local and international experience in the field of valuations.
- 2 Since inception of Corpcapital's investment in Cytech I have been intimately involved in Cytech's affairs and the developments in the online gaming and related industries worldwide. I have travelled extensively, virtually every month, to visit Cytech's operations and to attend industry conferences and numerous meetings regarding corporate opportunities relevant to Corpcapital's investment in Cytech.
- 3 I was responsible for the preparation of all Indicative Valuations of Cytech on behalf of Corpcapital for the purposes of determining the fair value of Corpcapital's investment for accounting purposes.
- 4 After Mark Matisonn joined Corpcapital in January 2001, he too was intimately involved in the preparation of the Indicative Valuations.
- 5 The sole purpose of the Indicative Valuations was to arrive at an honest and reasonable estimate of the value of Corpcapital's investment in Cytech. We did not inflate any of the valuations. Nor were we ever requested to do so.
- 6 For each valuation Corpcapital employed a valuation control process which ensured a series of checks and balances with the object of arriving at the fair value of the investment for the purposes of Corpcapital's financial statements. Briefly the process entailed the following:
  - 6.1 Financial information emanating from the business was carefully scrutinized and tested for integrity:
    - We had continuous interaction with operational management and a close proximity to the information emanating from the business.

- Monthly management accounts were submitted to us and were carefully considered by us.
- Monthly management meetings were held with the operational executives to analyse performance.
- We made monthly submissions to Corpcapital's investment banking executive committee meetings.
- We continuously kept executive directors of Corpcapital informed and in addition they had direct access to and regular interaction with operational executives.
- We, and other Corpcapital executives including executive directors, were closely involved with the corporate activities and opportunities relating to Cytech.
- As a result Corpcapital enjoyed a deep insight into the business.

6.2 Corpcapital's auditors, Fisher Hoffman (FH), played an integral part:

- For the financial year ending 31 August 2000 FH conducted a detailed review of the books and records of the business to satisfy itself that the underlying information and projections relied upon for the valuation were accurate and reasonable.
- For the financial year ending 31 August 2001 FH-conducted an audit of Cytech on behalf of Corpcapital in accordance with South African Accounting Standards (SAAS).
- For the financial year ending 31 August 2002 FH again conducted an audit of Cytech on behalf of Corpcapital in accordance with SAAS.
- FH concentrated its audit activities on the existence and valuation of Corpcapital's investments, specifically including Cytech.
- Each valuation was independently audited by FH for the purpose of expressing an opinion on the investment to

Corpcapital in accordance with SAAS. To this end FH thoroughly reviewed our valuation methodology and valuation assumptions and tested our conclusions for reasonableness.

- FH reported to the Corpcapital audit committee their satisfaction that the valuation was reliable and that their audit was sufficiently independent.

- 6.3 In preparing the Indicative Valuations Mark and I interacted extensively with other objective and technically proficient executive managers of Corpcapital (mainly Shane Kidd) and executive directors who had relevant knowledge and expertise (Jeff Liebesman, Martin Sacks and Benji Liebmann).
- 6.4 After completion of the Indicative Valuations they were subjected to further comprehensive consideration and debate, both formally and informally, amongst ourselves, Corpcapital's executive directors, representatives of FHS and members of Corpcapital's executive management involved from time to time in the preparation of Corpcapital's accounts. These further debates gave rise to the recommended fair value for purposes of the accounts.
- 6.5 In 2001 KPMG verified the valuations for the purposes of the Corpcapital group merger.
- 6.6 In 2002 PWC carried out an independent valuation of the investment.
- 7 The fair value of Corpcapital's investment in Cytech was capable of being measured reliably. To this end the discounted cash flow method of valuation ("the DCF Model") was appropriate. In addition the valuation was benchmarked against ascertainable market values for substantially similar investments and various Cytech specific corporate initiatives. The business had a track record and concrete business plans which facilitated reasonable projections and these were in turn capable of being tested against available relevant market information. In support of this:
- 7.1 The business commenced in May 1998 and started trading in December 1998. By August 2000 the business was highly profitable, cash generative with a large client base and an established brand.
- 7.2 By August 2000 the business was no longer an early stage venture capital start up. It had developed into a leading business in its industry and the

industry was widely regarded as an entrenched and growing component of the world economy.

7.3 Merrill Lynch, Credit Suisse First Boston, PwC (London) and other leading investment bankers actively analysed the industry and advocated the appropriateness of the DCF Model for valuing investments in the industry

7.4 The results produced by our DCF Model were evaluated against:

- Price/earnings and turnover valuation models.
- Valuations of comparable businesses, including their actual historic revenues.
- Corporate events and opportunities specific to the business.
- The independent views of FH and other Corpcapital executives.

8 I have never withheld or been a party to withholding any information from Corpcapital executives, the Corpcapital board or any non-executive director of Corpcapital (or its then holding company Corpgro). Corpcapital has a culture of open debate at all levels and its investment in Cytech was consistently the subject of such debate. When I became aware that Mr Frangos was querying certain aspects of the valuation I did not hesitate providing him with what he required. I was requested by Jeff Liebesman and later Martin Sacks to cooperate with Mr Frangos, which I did.

9 No member of Corpcapital's management or executive directors has any personal interest in Cytech, whether directly or indirectly. Sean Rose and Tal Harpaz are the beneficial owners of their combined 47.5% interest in Cytech. They are not nominal owners. The remaining 5% interest in Cytech is beneficially owned by Dawson Systems Limited. This share was previously owned by VR Services. This ownership is entirely at arms length.

The ownership structure of Cytech was well known and never the subject of disguise or speculation. In my discussions with Mr Frangos the ownership structure was referred to as a given fact and Mr Frangos never questioned the authenticity of the ownership of the 52.5% not owned by Corpcapital. I do not accept that the suspicion that he now casts thereon is genuine.

- 10 Mark Matisonn and I have carefully considered the valuation criticisms levelled by Mr Abrahams and Mr Collett in their reports. We are convinced that these criticisms are unjustified and that had they known all of the relevant facts and had the opportunity to consult with Corpcapital's management, they would not have arrived at their conclusions.
- 11 We have prepared and separately submitted to the inspectors:
- A document entitled "Cytech Valuation Report" which details in abbreviated form the facts relevant to each valuation.
  - An operational chronology of events.
  - A glossary of terms.

Mark Matisonn has prepared a separate statement for submission to the inspectors which I have read and agree with.

I ask that these documents be read as if incorporated into my statement.

- 12 For a complete understanding of the relevant facts and circumstances supporting each valuation it is necessary to consider my detailed statement and the separate documents referred to in 11 above. A summary of the relevant facts and circumstances at each material valuation date is provided hereunder as a convenient (albeit abridged) overview:

#### **August 2000**

- The business had grown exponentially in turnover and profitability.
- Market conditions were very favourable.
- Potential listings and merger opportunities were available. The indicative pricing of these opportunities was higher than our Indicative Valuation.
- The prognosis for the business and for the realisation of Corpcapital's investment was excellent

## **February 2001**

6

- Actual profits were ahead of forecast.
- The business continued to grow.
- The trend continued to be very positive.
- Relevant industry analysis supported all valuation assumptions.
- Corporate opportunities continued.

## **August 2001**

- The business was undergoing a fundamental change considered to be in its best interests and to enhance value, namely the change in the software platform resulting in a reduction of the software royalty and Aqua administration costs thereby significantly increasing profit margins.
- Historic revenue growth had flattened and future revenue was forecast to be 19% less than the prior year's actual revenue, to account for changes in the industry and primarily the change in the software platform.
- The US credit card issues were known but had not affected revenue and alternative payment mechanisms were anticipated.
- The business was expected to be more profitable off a lower turnover due to significant variable expense savings and its inherent value was regarded as enhanced by the improvement in the business model.

## **February 2002**

- All indications at that time were that the new software was well accepted by players.
- Forecast revenue was slightly less than the prior year's actual revenue
- The industry showed signs of softening

- The fair value was reduced by approximately 27% in US Dollars from that shown at August 2001.
- The reduction was a consequence of previously unforeseen changes in the industry and the business.

### **August 2002**

A valuation was carried out by PwC.

Our Indicative Valuation was within the PwC range of values.

The fair value accounted for was significantly lower than the February 2002 value due to continuing material changes in market conditions and unforeseen deterioration in the performance of the business.

- 13 In preparing my detailed statement I have carefully reviewed all of the relevant documentation and I have recalled the events of an intimate association over a period exceeding five years. It is difficult to do justice to the expose of that association in a written statement. I have not had as much time as I would have liked to make my detailed statement easily readable.
- 14 As he was intimately involved in the subject, Kevin Joselowitz has been requested to make a statement with regard to the restructuring of Corpcapital's investment in Cytech. I concur with his statement which will be delivered to the inspectors together with my statement.

**SIGNED at JOHANNESBURG on this the 1st day of OCTOBER 2003.**



**JADE HAMBURGER**

## J. HAMBURGER: STATEMENT

### INTRODUCTION:

1. My name is Jade Hamburger. I was born in South Africa on 3 September 1971. I matriculated with six distinctions from Damelin High School in 1989 and then went on to do a bachelor of commerce with a major in Accountancy (BCom (CA)) from the university of Witwatersrand. I graduated from my BCom with Honours (*Cum Laude*) in 1993 and then did my honours in Accounts (majoring in taxation). I qualified as a Chartered Accountant in 1996 after having served my three years articles at PriceWaterhouse ("PW" or "PwC") in Johannesburg.
2. My audit work focused on the banking industry. I specialised in the review of Bank's treasury operations with particular reference to derivative products. During my final year of articles I was seconded to work in the Corporate Finance department of PriceWaterhouse as an analyst.
3. Subsequent to completing my articles, I joined the Corporate Finance department of PriceWaterhouse (Johannesburg) as a manager in a full time capacity. My work focused primarily on merger and acquisition opportunities.
4. I was involved in valuation work including the valuation of Clover South Africa trademarks (R430m) on behalf of Group Danone pursuant to the acquisition by Danone of a strategic equity stake in Clover. Additionally, I valued the Zenex Oil trademarks (R280m) pursuant to a management buyout.
5. During 1997 I transferred to the London office of PriceWaterhouse Corporate Finance. The London office was the largest PW Corporate Finance office worldwide. My responsibilities included substantial involvement in the mergers and acquisitions aspect of Corporate Finance. I was involved in valuation work including financial valuations for and on behalf of the NHS Supplies Division of the NHS in England.
6. I left London to join the Corpcapital group ("Corpcapital") in July 1998. Corpcapital had recently been established. I joined the Investment Banking Division primarily with a mandate to initiate structure and maintain new and existing portfolio assets.
7. I am currently still concerned with the management of Investment Banking assets at Corpcapital.
8. I met Sean Rose ("Sean") and Tal Harpaz ("Tal") at university. The three of us lived together for approximately two years before Sean left to join Glencore (a commodity

## J. HAMBURGER: STATEMENT

trading business) in Switzerland. Tal and I continued to live together until he left to travel. Tal later settled in London.

9. The three of us kept in regular contact. Tal and I were living in London at the same time for approximately three months before I left London to join Corpcapital.
10. I met Evan Hoff ("Evan") at Wits and subsequently we both completed our articles at PW (Johannesburg). Evan was also seconded to the PW (Johannesburg) Corporate Finance department. We often worked together on joint assignments. Evan lived in the same street as Sean, Tal and myself and the four of us were close friends.
11. Martin Moshal approached Evan in early 1997, after Evan had completed his articles, to assist him in his online casino ventures. Evan left PW to join Martin. The internet was in its infancy at the time and I thought his move was brave.
12. The Moshal's had developed proprietary internet gaming software, which they branded under the name of Microgaming.
13. Evan became involved in the establishment of VR Services, an online casino management / administration company based in Cape Town. VR Services administered a number of Microgaming casinos.
14. Sean, Tal and I understood that VR Services supported casinos that were beneficially owned by the Moshal family.
15. Tal and Sean developed a business plan for the establishment of an online gaming company. Evan's proximity to the industry and his close relationship with Tal and Sean resulted in Tal and Sean being provided with first hand knowledge of the growth and profitability of the industry at the time.
16. The internet boom was just beginning. Online gaming was not yet widely regarded as the internet industry of choice. Evan's information was clear that, apart from the adult entertainment industry, online casinos were the perfect internet model and one of the few online industries to be profitable.
17. At the time Tal and I were living in London. Tal and Sean approached me to assist them in preparing a business plan motivating an investment in an online gaming operation.

J. HAMBURGER: STATEMENT

18. This business plan formed the basis of Sean and Tal's presentation to Corpcapital in May 1998 (refer V8<sub>2</sub> and V8<sub>217</sub>). Four key strategic strategies were identified by Sean and Tal in this presentation:
  - 18.1 The casino would be located in an offshore jurisdiction.
  - 18.2 The administration would be based in London.
  - 18.3 The Middle-Eastern markets (non-English speaking territories) would be targeted for growth.
  - 18.4 Microgaming was identified as the most likely casino software provider.
19. Sean and Martin Sacks are close friends. I met Martin through Sean. At the time Corpcapital was looking to employ executives and Martin approached me to join Corpcapital.
20. I joined Corpcapital approximately one month after Sean and Tal's presentation.

### THE INVESTMENT IN NETAINMENT

21. In or about June 1998, a decision in principle was made to invest in the online casino opportunity and I became involved in the implementation of the deal.
22. Corpcapital's motivation for making this venture capital investment was inter alia:
  - 22.1 The internet / technology boom was just beginning and Corpcapital wanted to participate in the expected growth;
  - 22.2 Through the association with Evan and VR Services, Corpcapital was given an inside track to the industry profitability and growth rates;
  - 22.3 The absolute size of Corpcapital's investment would be relatively small and the potential returns very high;
  - 22.4 Corpcapital was investing alongside individuals that were well known to Corpcapital.
23. The negotiations with Sean and Tal were protracted and strained. Sean and Tal were advised and assisted in the negotiations by Michael Segerman of Edward Nathan and Friedland CENF"). To fast-track proceedings a decision was taken by all parties to convert what was anticipated to be a non-binding heads of agreement into a binding contract
24. The investment was concluded and a binding heads of agreement was signed on 29 July 1998 (V8<sub>59</sub>) (the "GA Agreement") on the following material terms:
  - 24.1 The agreement was conditional on a due diligence, the conclusion of a VR Services consulting agreement and Reserve Bank approval;
  - 24.2 Three year service agreements;
  - 24.3 Sean and Tal were obliged to work with Corpcapital in the event of business failure (this mitigated the risk as we felt they would be good operators. Additionally, Corpcapital had medium term plans to expand overseas and Sean and Tal would be able to look for opportunities from London);
  - 24.4 A two-year restraint of trade following termination of employment;
  - 24.5 Total capital invested of \$600 000 consisting of \$40 000 from Sean and Tal and \$540 000 by Corpcapital. (Corpcapital was insistent that Sean and Tal contribute some of their own money to ensure commitment).

## J. HAMBURGER: STATEMENT

- 24.5.1 There were intense negotiations over the equity" split. Initially both Sean / Tal and Corpcapital each required 75% of the equity. A compromise of 50% was finally agreed. This joint ownership embodied the "joint venture partnership" relationship between the two parties and set the tone for the shareholder tension that would surface later.
- 24.5.2 Specific veto ability by Corpcapital; Rights of pre-emption, and come-alongs in favour of both parties;
- 24.5.3 An agreement with VR Services was contemplated. It was agreed that VR Services would be entitled to up to 5% (non-voting) equity of the casino business (only) in lieu of fees;
25. The GA Agreement contemplated that for the purpose of valuation of "shareholders interest" the fact that an interest constitutes a minority would be ignored.
26. A clause was incorporated stating that "the parties will maintain the utmost confidentiality regarding the conclusion and content of this Agreement and in due course the Definitive Agreement save only for such disclosures and announcements which are required to be made by law or which are previously approved in writing between the parties". This clause embodied the desire by Sean and Tal to maintain a level of secrecy around the dealings in this asset (primarily for personal tax considerations on their part). In subsequent years Sean and Tal criticised Corpcapital for disclosures it made to the press (V21<sub>17</sub>).
27. The binding GA Agreement contemplated a separate shareholder's and definitive (comprehensive) agreement agreement. A draft shareholders agreement was circulated by ENF but the parties never concluded this. The definitive agreement contemplated in the GA Agreement was never attempted. The GA Agreement however effectively governed the relationship between the shareholders and still does so.
28. *In November 2000 Sean and Tal demanded that, given the recent business success (the formation of Aqua the anticipated English Harbour merger) they felt it was appropriate to be released from all outstanding obligations contained in the GA Agreement. Corpcapital was not prepared to do this. As usual there was a lengthy internal Corpcapital debate and disagreement with Sean and Tal over this issue. We resolved to settle the matter by substituting the GA Agreement with similar rights and obligations contained in a new Netainment shareholders agreement. Sean and Tal instructed Larry Nathan of (Mishcon De Reya ("Mishcon'l (a prominent London law firm) to comment on Kevin Joselowitz's draft*

## J. HAMBURGER: STATEMENT

*agreement. This agreement was debated for months but never signed. Various drafts are contained in the Cytech submission pack. The GA Agreement therefore continued to regulate the relationship.*

29. After signing the GA Agreement, on behalf of Corpcapital, Benji submitted a memorandum to First National Bank ("FNB") in support of an application for SARB approval, as part of Corpcapital's strategy to expand its overseas interests
30. The Reserve Bank raised queries in response and FNB expressed to Benji their view that the application would be better received by SARB if it was made by a company operating in the IT industry rather than an investment bank because SARB was generally reluctant to permit investment abroad by investment banks.
31. At the time we received this response, discussions for Corpcapital to establish an investment into a separate e-commerce entity, were well advanced. These discussions were the precursor to the establishment of Aqua. The SARB application by Corpcapital was put on hold pending the outcome of these initiatives.
32. Subsequently when Global Admin and Interactive were acquired by Aqua SARB approval was sought and obtained.
33. As a consequence of these transactions Corpcapital was entitled to receive its 47.5% and 50% interests in Netainment and CFI for no consideration as these companies were excluded from the sale to Aqua.
34. Corpcapital's right to receive its interest in Netainment and CFI was reported to SARB in accordance with the Regulations. This notification was handled by Kevin Joselowitz of Corpcapital Corporate Finance and Benji. SARB responded by approving Corpcapital's interests in Netainment and CFI, imposing thereon its usual conditions applicable to offshore investments.

**THE ESTABLISHMENT OF THE OPERATIONS**

35. After negotiating and concluding the GA Agreement, Sean and Tal returned to London and established operations in Kentish Town. They developed the call center and back office administration infrastructure necessary to support the operations of internet businesses (and specifically online casinos).
36. They established Global Admin (a UK company) to house the London based operations. Interactive Online (a BVI company) was established to provide consultancy services to internet businesses. Corpcapital received a right to own 50% of these operations (that it later converted into Aqua shares).
37. The agreement with VR Services (as contemplated in the GA Agreement) was signed in August 1998 (V8i<M). This agreement entitled VR Services to earn up to 5% of the casino business (which was ultimately housed in Netainment and not Global Admin).
38. VR Services received its equity in lieu of fees for providing consulting services to the startup business. VR Services advice pertained to inter alia necessary hardware infrastructure, designing of relevant internet marketing plans for the casino business, setting up internal control procedures and other technical support. This advice was invaluable and ensured that the many teething problems and mistakes normally experienced by a start up business were avoided. Specifically, given the success of the marketing strategies, the casino was able to trade profitably very soon after its initial launch.
39. The 5% earmarked for VR Services was envisaged in the GA Agreement and VR Services Agreement to be non-voting. VR Services ultimately transferred its shareholding in Netainment to Dawson Systems Limited (V9<sub>51</sub>).
40. At the time of conclusion of the GA Agreement Benji noted that it was important for Sean and Tal to determine an appropriate corporate structure for the business. In this regard Sean and Tal obtained an opinion from Mishcon on issues of taxation and jurisdiction.
41. It was not legal for a London based company to own and operate an online casino. Sean and Tal therefore established Netainment (a Netherlands Antilles company) for this purpose. It was agreed that Corpcapital would own 47.5% of Netainment, Sean and Tal 47.5% and VR Services the remaining 5%.

## J. HAMBURGER: STATEMENT

42. Netainment applied for and received a licence to operate an online casino in Antigua. Netainment's gaming servers were then physically transported to Antigua in order to comply with the Mishcon opinion regarding gaming jurisdiction.
43. CFI (a BVI company) was formed to establish banking relationships to facilitate e-commerce financial transaction processing. It was agreed that Corpcapital would own 50% of CFI and Sean and Tal the other 50%.
44. The Global Admin infrastructure was initially established to support the operations of Netainment. In time it became apparent that Global Admin was capable of supporting other brands of casinos and different types of e-commerce companies. Even before Netainment's first casino (branded King Solomon) went live there were opportunities to support other online businesses including lotteries, online UK book retailers, UK horseracing pools (V8<sub>117</sub>). Global Admin began to develop a customer base of clients in addition to Netainment. This was consistent with the original investment strategy.
45. There was and never has been any doubt that Sean and Tal are the real beneficial users of 47.5% of Netainment (now Cyteoh) and 50% of CFI or that VR Services (subsequently through Oawson Systems is the real beneficial owner of 5% of Netainment (Cytech). (Please refer to additional information to this topic in Appendix 5).
46. Internet business was booming and opportunities were plentiful. Loss making companies like AOL were valued in excess of \$27 billion.
47. An online casino requires gaming software to operate. Sean and Tal researched the market and concluded that Microgaming offered the best product.
48. In December 1998, the Microgaming license contract was concluded ("MGS agreement") (VBz0s). The negotiations with Microgaming ("MGS") (represented by Martin Moshal) were difficult. Moshal was unwilling to vary MGS's standard commercial terms, which were onerous. Microgaming required Sean and Tal to be restrained from running a casino operation in parallel to the Netainment casinos (i.e. alternative casino software platforms were forbidden).
49. The MGS agreement contained the following terms inter alia:
  - 49.1 A royalty of 25% of Gross Win ("drop" / "revenue");
  - 49.2 The agreement was "continuous", containing no fixed terms or notice period. The legal advice received at the time was that the agreement could be terminated giving reasonable notice ("reasonable" was assumed to be a few months).

**COMMENCEMENT OF OPERATIONS**

50. Netainment commissioned the development of its website and the establishment of its call centre infrastructure. Global Admin implemented this. The King Solomon brand was the first casino to be established by Netainment.
51. The online casino commenced operations in December 1998.
52. Around November 1998, Schindlers (a trust company based in London and Lichtenstein) were appointed to assist in the administration of the corporate structure and become the initial corporate directors for Netainment, CFI and Interactive.
53. Tal and Sean were conscious of the advice they have received to establish an efficient corporate structure. They commission arm's length agreements between the various corporate entities. Market related service contracts between Netainment, Global Admin and Interactive were concluded.
54. At the time of going live in December 1998 the online gaming market was immature. The size of the market dwarfed the number of serious casino operators and was growing faster than the internet at the time. Almost any casino established around this time with modest capital was able to turn a profit if it offered an average product. The "Microgaming casino platform was very popular with online gaming players.
55. The American market was the "low hanging fruit" of the casino industry at the time. Like motet of its competitors, Netainment focused a large portion of its marketing resources at the American market. At the time it seemed that the growth in the business would be constrained only by the extent of the money you were able to spend on marketing.  
Revenue and profit were directly proportional to marketing spend.
56. Infrastructure is a fixed cost. The variable costs at the time were the MGS royalty and transaction processing fees. The casino product was delivered electronically. Additionally, the business carried no stock and received cash in advance from. Players, Apart from the upfront costs to establish the infrastructure, ongoing capex spend was minimal. Player loyalty meant that as the business expanded its margins grew. This is the perfect business model. Although there is natural player attrition in the casino's database, a core number of new players attracted each month by the marketing spend remained with the business for years. If the casino were to stop marketing in a month, these players would deliver revenue almost directly to profit (after the variable costs).

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57. In subsequent years, increased competition and credit card issues created barriers to entry in the market (it became harder to deliver a profitable return from advertising). New entrants required an established "real world" brand or extensive capital to develop an internet brand if they wanted to survive.
58. Netainment with its early first mover advantage into the industry was able to quickly establish a database of players and an internet brand name to enable it to overcome the difficulties in the industry that happened in later years.
59. Netainment recognized early however that it could gain a competitive advantage by targeting unique countries with language specific content and call center support.
60. Tal was born in Israel and was very familiar with the country. This was fortunate for the business. Netainment began to actively target the Israeli market with a Hebrew version of its King Solomon brand almost from inception. This proved to be the most important strategic initiative of the group as the Israeli market has a high propensity to gamble and is particularly loyal. King Solomon was able to develop a dominant market position in Israel. The player return from advertising spend in Israel was (and still is) particularly high.
61. The Hebrew version of King Solomon's is a well-known brand King Solomon's was identified as the third most recognized gaming (not just online) brand in the country and has a strong competitive advantage to other gaming products. The Israeli customer base is particularly high margin and loyal.

**EARLY INDUSTRY REPORTS AND BUSINESS STRATEGY**

62. Press articles detailing the attractiveness of the online gaming market began to filter through to Corpcapital from 1999.
63. Jeremy Badstone of Natwest Stockbrokers (whom I called and spoke to telephonically) was very bullish about e-gambling (V9<sub>13</sub>).
64. Corpcapital identified early in the life cycle of the industry that land based gaming brands like Ladbrokes and Lasseters, and personalities like Kerry Packer would begin to develop online gaming strategies. In our opinion, the emergence of the 'brand names" legitimised our gaming investment and the industry (and confirmed our knowledge of its attractiveness)
65. Additionally these brand names reinforced our belief that the industry would ultimately regulate.
66. The casino's corporate strategy at the time was to ultimately exit to a land based property that wanted to migrate online. Alternatively, and more attractive, was the strategy to create the necessary critical mass to purchase an established branded land based operation. This last idea was particularly appealing after AOL and Time Warner merged in February 2000.
67. A report by me on the performance of the casino was included in the Corpgro board pack (V9<sub>29</sub>). It is clear from this report that the operations were profitable almost from inception (operations commenced four months previously).

**ESTABLISHMENT OF AQUA**

68. The Global Admin business had developed independently of Netainment
69. Around March or April 1999, the concept of creating a dedicated e-services group to be listed on the JSE was developed.
70. Alex Maraney and Wayne Brett introduced Corpcapital to a small, young e-services company called Apshai. Internationally, comparable companies like Sapien, Razorfish and Scient were big brand names and highly regarded by the financial market. I identified a similar but larger business run by Brent Shahim called Aqua Information Station. These two companies provided consulting, design and IT services specifically focussed around internet technologies.
71. A strategy was developed to combine Apshai and Aqua Information Station, rebrand the merged business, reverse-list the company and then consolidate and grow organically and through acquisition. This industry roll-up strategy had been successfully implemented by Corpgro in the outdoor advertising market with its consolidation of businesses into Corpcom.
72. It occurred to Corpcapital that to be successful in providing e-services, an internet centric service provider should be able to extend its services to include website administration and financial transaction processing.
73. Global Admin and Interactive were busy developing its businesses into a provider of administration and consultancy services to "dot.com" companies (primarily online casinos but it also had other clients).
74. There seemed to Corpcapital a natural fit between Apshai/ Aqua and Global Admin/Interactive as the combined company could offer its clients an extended range of e-commerce services. Additionally, given Global Admin/ Interactive's access to hard currency world markets, the South African based divisions could provide rand based (but world class) services to hard currency paying clients.
75. Corpcapital was conscious at the time of developing an e-commerce business that would make significant profits (in an industry where loss making companies were attracting high ratings). Benji in particular was insistent that the loss market dot.coms would ultimately fail and their shortcomings be exposed to financial markets.

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76. Notwithstanding resistance from the Aqua executives the Aqua Online revised listing particulars contained a profit forecast (as opposed to forecast of losses, in the hope of achieving a turnover multiple based valuation, common with international markets at the time)
77. At the time of Aqua's reverse listing all of the underlying businesses were profitable and growing.
78. The acquisition by Absec (the cash shell) of the Aqua Information Station / Apshai and Global Admin / Interactive businesses was announced to the market on 4<sup>th</sup> of August 1999.
79. Aqua's revised listing particulars were only released in April 2000 given the protracted negotiations with the Reserve Bank for approval to acquire the international businesses.
80. The Absec General meeting to approve the Aqua acquisitions was held on 12 May 2000.

**ACCOUNTING POLICY**

81. Soon after joining Corpcapital I participated in discussions and research regarding the appropriate accounting treatment for Corpcapital's investments. I held discussions with PWC who gave me a verbal opinion on the matter. I also discussed it with Fisher Hoffman ("FH") (Corpcapital's auditors). FH produced a draft opinion a relevant forecast. Together we reviewed the prevailing GAAP statements and international accounting standards. We also had regard to market commentators' reports which said that international best practice was for investment companies to mark their investments to market and reflect increases and decreases in their income statement.
82. The uniform conclusion was that this was the best accounting practice and that accordingly Corpcapital would adopt it.
83. The investment in Netainment was treated in this way, along with Corpcapital's other investments. A fundamental tenet of this decision was the recognition that the investments, including Netainment, were all held for sale in the near future.
84. In relation to each valuation that followed of Corpcapital accounting purposes, I was satisfied that Corpcapital's investment in Cytech was capable of being measured reliably and I was satisfied that the indicative valuations presented by me for review by the executive management, directors and auditors, constituted a reasonable estimate of the value of the investment.

**THE FIRST VALUATION (AUGUST 1999)**

85. In August 1999 I produced my first valuation of Netainment (V9<sub>47</sub>). A valuation of \$3m (100%) was determined based on a forward PE ratio of 3x on annualised August 1999 profits. Listed comparable multiples of 58x and 19x were noted in the market for Boss Media and Tropika respectively. Casino profits were growing exponentially per month and I calculated an annualised earnings based on the last month's profits on which to apply the multiple.

J. HAMBURGER: STATEMENT

**THE EVENTS LEADING UP TO THE FEBRUARY 2000 VALUATION**

86. In January 2000 the first Bear Stearns report was released (refer V3<sub>1</sub>). The report is very comprehensive. The following information from the report was key to our understanding of the industry at this time:

The online gaming market was forecast to grow by 80% per year until 2002 and beyond.

86.1 They do not believe the Kyl" will pass although they do feel that other forms of legislation will be proposed to regulate internet gambling (as opposed to prohibit it).

86.2 Certain established jurisdictions were beginning to recognise and support the industry.

86.3 Online gaming companies, like any internet company, were able to leverage off economies of scale. Infrastructure costs of internet businesses are relatively fixed (or stepped in nature) and e-commerce companies are able to increase revenues without a dramatic increase in cost. The result is that operating margins in e-businesses should increase over time (we initially experienced this with Netainment. This was also consistent with the VR Services experience).

86.4 The industry had low barriers to entry but the development of established brands should create an artificial barrier. King Solomon's have managed this successfully in non-US markets, notably Israel.

86.5 "Internet gaming firms will be able to raise their market capitalisation and share value when the industry legitimises itself within the US" therefore industry players should welcome regulation

86.6 "consolidation will be a key factor driving the future of the industry, but branding will continue to be of utmost importance". (King Solomon already enjoyed a strong brand).

86.7 King Solomons.com was listed in the Bear Stearns report (V3107).

87. By January 2000 Sean and Tal believed that the casino business had substantial growth potential. They recognised that the business was growing in multiples of the amounts spent to market the brands. Sean and Tal approached Corpcapital to provide debt funding to the business to finance this growth. Sean estimated future monthly growth in the business to be exponential based on recent history. (V10<sub>114</sub>)

## J. HAMBURGER: STATEMENT

88. Jeff and Benji were directly involved in evaluating this proposal and obtained an inherent understanding of the potential of the casino's cash generation ability. Benji did not favour the funded growth strategy, preferring a more conservative balance between growth and free cash generation.
89. In January 2000 William Hill investigated listing its online betting operations. This was further evidence of an established "UK brand" mitigating online and listing on the UK exchanges.
90. Sporting bet.com released their interim results. Its market capitalisation was £160m. The business turned over £4.6m and lost approximately £1m. Sportingbet offered predominantly online sports betting but this was regarded as a good proxy for online gaming valuations.
91. By January 2000, approximately 50% of the casinos business was derived from non-US sources. The return on marketing spend outside America was far better than US advertising returns. I recognised at the time that Netainment would have higher operational margins than its competitors because of this. Additionally, I had an early premonition that the industry would one day mature but I was not sure when this would happen (refer V3izg). The statistics I included in this memo to Benji clearly indicated that the business was growing rapidly and profitably.

J. HAMBURGER: STATEMENT

**THE FEBRUARY 2000 VALUATION**

92. In February 2000, the business was valued at \$5.7m (100%). This was based on the growth experienced by the company, a PE of 7 and an exchange rate of 6.3 (V IO<sub>135</sub>)

J. HAMBURGER: STATEMENT

**THE EVENTS LEADING UP TO THE AUGUST 2000 VALUATION**

93. By the beginning of the year 2000, the dot.com listings boom was in full swing on the London stock exchanges. Corpcapital felt that to unlock the value of its investment in Aqua and Netainment and to obtain a listed currency for Netainment acquisitive growth strategies, it would require a London listed presence for these businesses.
94. Industry trade journals (Red-Herring) justified PE ratios in excess of 100x for listed internet companies on the basis that e-commerce companies exhibited exponential growth (V10<sub>180</sub>). These multiples were not unusual for the time.
95. Corpcapital firmly believed that a London listing was an attractive strategy for its internet assets for the following reasons:
- 95.1 There was a strong investor appetite for internet stocks at the time;
  - 95.2 London was proving to be a jurisdiction that supported online gaming companies (Sportingbet, Gaming Internet).
  - 95.3 Netainment and Aqua were profitable, cash generative and growing. This, we felt, was a unique selling point relative to the other internet listings that were 'burning'<sup>1</sup> cash.
  - 95.4 The London listing would facilitate a consolidation strategy, using paper for acquisition of comparable businesses.
  - 95.5 Sean and Tal were physically based in London.
  - 95.6 A listing would enable Corpcapital to exit its investment optimally.
96. There were three London listing initiatives to list on AIM or the LSE through an IPO or reverse-listing namely:
- 96.1 An e-commerce group listing (V10<sub>211</sub>). (consisting of a merged Aqua, Netainment and CFI business). This was not well supported by Sean and Tal.
  - 96.2 A separate Netainment listing. This was supported by Sean and Tal; and
  - 96.3 A separate Aqua listing promoted by the executive Aqua board of directors
97. Insinger Townsley (*who later pitched for the sponsoring broker role for the Netainment London listing*), released its internet stocks research report (V10<sub>240</sub>). This report detailed the prevailing London listed pricing values. Additionally, the report detailed the prospects of Gaming Internet (V10<sub>255</sub>) a direct competitor to Netainment.

## J. HAMBURGER: STATEMENT

98. In March 2000 I dealt closely with Doug MacDonald (a deal broker) who was eager to introduce Netainment to institutions in London (V11<sub>8-11</sub>). He informed Corpcapital (Benji and me) about current strong demand for AIM listings (particularly in the internet sector). He also mentioned there should be no resistance to an online gaming listing (which was a concern that we had at the time).
99. The press at the time confirmed that the Netainment corporate structure was not unique (V11<sub>11</sub>). Sportingbet.com for example, had established operations in the Channel Islands.
- 99.1 Mark Blandford (from Sportingbet.com), in this RedHerring article, confirmed my thinking at the time that the online gaming industry would regulate and that the young, recently established online gaming brands would establish a first-mover advantage in the internet gaming space long before the land based competitors entered the market.
100. DataMonitor, a London based research group, predicted that online gambling would be a \$5.5 billion market by 2001. Their forecast in online gamblers was expected to double annually.
101. These reports encouraged us. It was clear that the London financial markets were receptive to online gaming and internet opportunities. Sean and Tal were based in London. We were bullish that a London listing could be successfully achieved.
102. In April 2000 Jeff went to London to meet with various promoters, sponsoring brokers and investment banks to investigate the London listing of our e-commerce assets. In April 2000, I flew to London to visit the operations and follow up on the listing initiatives started by Jeff.
103. The good progress made in London at the time prompted Benji's memo in April 2000 (V11<sub>14</sub>). This memo summarised the importance of the proposed listing transactions to Corpcapital and all stakeholders at the time. Additionally prevailing governance issues were highlighted. The following points are extracts from the memo.
- 103.1 Corpcapital needed to be conscious of conflict of interest issues at all times;
- 103.2 Sufficient diligence was to be placed on the valuation process for the purpose of any capital raising. I was instructed to analyse international pricing models and prepare forecast earnings. Additionally it was anticipated that these valuation methodologies might be tested by London sponsoring brokers looking to place capital for the company in contemplation of a listing. I was therefore advised to be prepared to defend calculations at all times. *(Benji is particularly fastidious on matters of process. As a result I kept detailed records and provided regular feed*

## J. HAMBURGER: STATEMENT

*back to ensure that Benji (and later Martin, Jeff and Shane) were always updated about developments).*

- 103.3 Project Management of the listing process was considered vital (information needed to be comprehensively prepared and efficiently distributed, confidentiality was to be adhered to at all times and due attention need to be given to timetables, agendas and minutes).
- 103.4 It was noted that all contractual, statutory and regulatory compliance issues needed to be dealt with (Benji lists some of them).
- 103.5 Benji was conscious of the distracting nature of a London listing and emphasized the need to stay focused on the Aqua JSE listing initiatives and management of the operational business.
104. I established a project management framework to consider the listing and began a process of weekly Netainment listing steering committee meetings. (V11<sub>31</sub>). I prepared regular status reports (V11<sub>53</sub>; V11<sub>51</sub>) and minuted all meetings (V11<sub>195</sub>). The documents were circulated to all members of the project team including Kevin Joselowitz, David Leibowitz, Benji and Jeff. Corpcapital Corporate Finance was engaged to advise on two matters that could arise as a result of the London e-commerce initiatives; namely conflict of interest issues (V11<sub>209</sub>) and exchange control issues (V11<sub>215</sub>). We were highly aware of these concerns at the time.
105. There were various corporate listing opportunities that presented themselves for both Netainment and Aqua during the period April to August 2000. I took the presence of these opportunities into account in my assessment of market conditions for the purpose of my valuations. The various alternative listing opportunities were:
- 105.1 In May 2000 Insinger Townsley (a London based sponsoring broker) pitched to list Netainment on the AIM market in London. Insinger believed that they could raise between £3m - £5m new capital at a pre-new-money valuation of between £30m - £50m (\$50m - \$83m). They recommended a placement at a price acknowledged to be lower than market value in order to give initial outside investors (their clients) a good profit opportunity and thereby create an active market for the remaining listed shares (V11<sub>201</sub> and V11<sub>204</sub>).
- 105.2 Reverse listing of the e-commerce group into a London cash shell (Crestan);
- 105.3 E-commerce group Aim listings (discussed with sponsoring brokers Warburg, Henderson Crosswaith, J P Morgan, Salomon Bros, Merrill Lynch and Insinger Townsley);

## J. HAMBURGER: STATEMENT

- 105.4 Preliminary investment interest in Netainment expressed by Investec on behalf of fcs client BskyB;
  - 105.5 Doug McDonald initiatives (discussed earlier)
  - 105.6 In June 2000, Jonathan Schneider advised the non-executive board of Aqua of his initiatives to merge Aqua with Amaze. Amaze had a valuation of approximately £45m. At the time Jonathan was arguing that the Aqua share price, given the thin volumes, undervalued the true market capitalisation of Aqua;
  - 105.7 In July 2000 Jonathan Schneider advised that Beeson-Gregory were eager to assist Aqua to list on AIM. Beeson had confirmed an initial valuation on the Aqua business of between £35-40m. Additionally they indicated an appetite in the London market for a fund-raising of between £5-1m. Notwithstanding the differences in the Aqua and Netainment businesses, this gave us a strong indication that the London market was still receptive to internet listings at this time and that company valuations were still trading on high multiples. Aqua was trading at a market capitalisation of approximately R250m at the time.
- 106. The interest in Aqua (noted above) fortified our assessment that the financial markets (particularly London) were hungry for e-commerce opportunities at particularly attractive valuations.
  - 107. In early May 2000 Sean informed Corpcapital of a potential opportunity to merge the Netainment operations with a Canadian based online casino called English Harbour. A complete chronology of the English Harbour negotiations is contained in the Appendix 9. Notwithstanding the signing of a binding merger agreement, the English Harbour merger (to form a company called "Amalco") was ultimately not pursued as the consent of Microgaming, a condition precedent to the deal, was refused.
  - 108. The key relevant facts arising out of the English Harbour negotiations for the purpose of this statement are:
    - 108.1 The opportunity presented was for Netainment to merge its business with a larger industry player;
    - 108.2 Notwithstanding that Netainment's results were smaller than English Harbour's, Corpcapital, Sean and Tal managed to negotiate for 50% of Amalco (primarily because of the higher non-US player component of the business);
    - 108.3 This transaction provided valuable insight into a competitors' business validating Corpcapital's growth assumptions for the industry and Netainment. Corpcapital

## J. HAMBURGER: STATEMENT

was able to analyse the English Harbour financials as a result of discussions with English Harbour executives (predominantly Paul Sudolski the CEO) and the subsequent due diligence investigation performed on the English Harbour business;

- 108.4 The parties considered an Amalco listing on the London AIM exchange highly achievable within a year of the merger
  - 108.5 The merger anticipated that Aqua would service Amalco at fees approximating 6% of Amalco revenue, in line with the existing English Harbour infrastructure costs (this was a reduction of the then current 12.5% fee levied by Aoua on Netainment's revenue);
  - 108.6 English Harbour and Netainment were the subject of mutual due diligence reviews that were satisfactorily concluded.
109. In May 2000 I received an instruction from the Investment Banking Exco to have an independent expert value the Netainment asset. Please refer Appendix 4 for a detailed account of the "External Valuation" chronology. The result of the process was a decision by the Corpcapital board not to proceed with the substantial expense of a third party valuation, given the Corpcapital's internal expertise and the roll played by Corpcapital's auditors to audit the internal valuation.
110. In my July 2000 (V11<sub>305</sub>) investment banking Exco report, I commented on Netainment's June 2000 results and noted that revenues were slightly up by 10%. *My choice of words indicates that I believed a 10% monthly increase was a slight improvement in performance.* Profit, however, was down (as a result of large marketing spend). July's results were forecast to improve substantially. I understand and mention that a potential reason for month-on-month volatility in profits may be a result of matching issues relating to the accounting for marketing expenditure. This is due to the following factors:
- 110.1 Marketing spend in a month may only yield returns in future months. Players attracted in month one may only start playing actively in subsequent months.
  - 110.2 Marketing payments were sometimes prepaid. The business would be pay in advance for a campaign that would run over a few months.
111. The above points are important to consider when understanding the valuations. It is necessary to determine the trend in profits over a period rather than. It is difficult to comment on one month in isolation. Additionally as this is a casino business there is always an inherent volatility of a player winning an abnormally large amount in a month. Over time these effects are neutralised to give a true reflection of performance (i.e. a trend).

## J. HAMBURGER: STATEMENT

112. Stanley Leisure released its annual results (V12<sub>138</sub>) with a 32% rise in earnings. Additionally, the company commented on the initial success of its internet casino acquisition and stated that they believed this business was a growth area for the company.
113. Industry press at the time July 2000 (V12<sub>136</sub>) reinforced the thinking that it would be difficult to enforce any legislative ban on on-line gaming.
114. On July 20<sup>th</sup> 2000, the House of Representatives failed to pass a bill banning internet gaming. (V12<sub>158</sub>). This further reinforced Corpcapital's thinking that the industry would continue to maintain the current status quo for the foreseeable future.
115. Starnet Communications International (market cap of \$83m) announced in July 2000 that it was launching a Chinese internet gaming site. This indicated that there was a potential Asian market worth pursuing. (Netainment subsequently, yet unsuccessfully launched a Korean website in April 2002.
116. The Credit Suisse / First Boston analyst reports on Stanley Leisure was noted in August 2000. The relevant analyst commented that Stanley Leisure was a "strong buy" noting that future growth would come from the recent online gaming acquisitions. These reports confirmed our conviction that the London financial market identified and valued the importance of land based gaming operations that developed online casino strategies. Stanley Leisure's WACC was 7.6% at the time. *(The Stanley Leisure acquisitions are dealt with more fully in the "Cytech Valuation" document).*
117. In September 2000 the second largest Israeli newspaper Ma'ariv published a list of the most widely recognised gaming brands in Israel. King Solomon's was voted third behind the state run lottery and sports betting business. This confirmed our belief that the Hebrew version of our online casino was a dominant brand in its Israeli market. It explained our success in the region and reinforced our confidence of the intrinsic value of the business.
118. A bullish BOE securities brokers report dated 26<sup>th</sup> September 2000 was released with respect to Aqua. BOE recommended a strong buy. The indicative forecast PE ratio used by BOE for the purposes of their Aqua valuation was 21x (V13<sub>405</sub>).

**THE AUGUST 2000 VALUATION**

119. In the beginning of August 2000 I developed the financial model used to determine the indicative valuation of Netainment.
120. The importance of this first valuation was debated at various investment banking operational meetings and Investment Banking Exco meetings.
121. This was Corpcapital's first attempt at a comprehensive discounted cash flow ("DCF") valuation of the Netainment business. The executive directors and I were very conscious of its importance given the material nature of the asset.
122. I was particularly aware that this valuation would provide a benchmark and framework for all future valuations. The methodology would need to be consistently applied in future periods.
123. Additionally, my valuation methodology and assumptions would need to withstand scrutiny from within Corpcapital and from our auditors. (Additionally, when I developed the August 2002 valuation model I believed we were going to get an external advisor to prepare an independent valuation).
124. I had previous experience (as noted earlier in this statement) in performing valuations at university, PwC Johannesburg and PwC London. At the time of preparing the model I performed research that consisted of a review of my university textbooks and previous valuation financial models used at PwC to ensure that the methodology used was appropriate.
125. I spent a lot of time consulting with Shane (who has a strong technical ability) to refine the model.
126. *Please refer to the process for preparing and reviewing the valuations contained in the Appendix 2.*
127. My research and experience led me to the conclusion that a discounted cash flow basis of determining value was the most appropriate valuation model. Netainment was no longer a start-up company. By the time of the August valuation it had a track record of increasing turnover and cash profits. In this regard I refer to the document titled "Cytech Valuation". In addition the following factors were evaluated by me:

## J. HAMBURGER: STATEMENT

- 127.1 DCF is recognised as conceptually the most appropriate method of valuing a business. It is particularly relevant for cash generative, high growth businesses that require little re-investment / capex for future growth.
- 127.2 An earnings yield or PE valuation cannot adequately provide for future anticipated changes in the business. Future events like the renegotiation of Aqua fees, change in royalty basis or movement in operational margins can never be adequately dealt with using a comparable multiple approach.
- 127.3 PE valuations use comparable data businesses and indices that are not strictly comparable.
- 1 27.4 Turnover and earnings multiple basis were, however, performed to benchmark the DCF value.
- 127.5 The PwC (London) valuation proposal (referred to in Appendix 4) provided a useful indication of the methodology they would recommend to value Netainment. PwC proposed performing a valuation based on a discounted cash flow analysis (V11<sub>404</sub>) supported by an analysis of multiples from comparable listed companies.
- 127.6 The ABN Amro Broker's report at the time of the Aqua listing (check date) (V11<sub>255</sub>) supported a DCF basis of valuation. ABN Amro note that "the valuations of e-commerce and internet-related players are increasingly difficult to determine given the disparities in demand forecasts and the evolving business model". Notwithstanding, they propose two techniques to determine fair value being a discounted free cash flow and the PE Relative method. In performing their DCF valuation, ABN Amro determined the discount rate using the CAPM model.
- 127.7 *I point out that the use of the DCF model was subsequently confirmed as appropriate in the Merrill Lynch report (January 2001) (V18<sub>169</sub>).*
- 1 28. In respect of the August 2000 valuation:
- 128.1 circulated the indicative valuation document to Benji, Martin, Shane and Jeff for their comments and discussion. I clearly marked the first draft as such and mentioned to Benji that the values would be adjusted after debate and discussion. I was aware that all my assumptions would be tested and debated for reasonableness and conservatism. This occurred in a series of meetings with Shane, Benji, Jeff and Martin referred to in the various email correspondence. The first draft of my August 2001 indicative valuation is contained in V13<sub>55</sub>.

J. HAMBURGER: STATEMENT

128.1.1 *This draft version was inadvertently given to Mr Frangos in my submission to him of 21 June 2002 (V20243) instead of the final version referred to below.*

128.2 Benji commented on this first draft in a memo dated 14 August 2000 (V1392). He mentioned that the numbers had not been reviewed and re-iterate the point that FHS must perform sufficient and adequate work on the accounts prior to finalisation of the valuation.

1 28.3 I asked Benji and Shane for further comment on my Netainment valuation prior to a meeting scheduled with Jeff on August 15 (Jeff, Shane and myself attend) (V1394.). Additionally, on August 17 the Netainment valuation was debated with Peter Katzenellenbogen ("Key"), Shane, Jeff and myself. Although I cannot recall specifically what was said in this meeting, I have no doubt that we debated the methodology for valuing the business and determined appropriate audit tests to ensure that the value was based on accurate financial information and assumptions.

1 28.3. 1 *I included the narrative summary of the indicative valuations in my submission to Mr Frangos of 21 June 2002. I did not include the Excel models part of the valuation workings. There was nothing sinister in this omission. It is clear to a reader of the narrative that there is a detailed financial model to support the calculations of the valuation ranges. I would have provided these models to him if he requested them.*

129. After interactive exchanges between me, Shane, Martin, Jeff, Benji and Peter Kay I finalised my August 2000 indicative valuation in September 2000 (V13<sub>55</sub>)

1 30. A summary of the key business drivers of the indicative valuation at this date were:

1 30.1 The business had grown exponentially in both turnover and profitability.

1 30.2 Market conditions were very favourable.

1 30.3 Potential listings and merger opportunities were on the table.

1 30.4 The prognosis was excellent

131. In August 2000 the fair value of the business was determined to be \$44.8. m (100%) and \$21. 3m (47,5%) (V13<sub>55</sub>). Please refer to the "Cytech Valuation" document for further detail.

## J. HAMBURGER: STATEMENT

### THE EVENTS LEADING UP TO THE FEBRUARY 2001 VALUATION

132. My Investment Banking Exco report dated 24 October 2000 (V13<sub>84</sub>) contained the following relevant information:
- 132.1 I noted that the Aqua term sheet had been negotiated with Amalco.
- 132.2 The Fisher Hoffman review of the Netainment management accounts identified no material issues.
- 132.3 Sean Rose will move to Netainment on a full time basis from 1 December.
- 132.4 I believed that a 3% month-on-month increase in actual revenue was relatively moderated. My state of mind was that a compound 43% per annum increases in revenue was only a moderate performance given the history of exponential growth and very favourable market conditions and prospects at the time.
133. The date of this report is important because it shows that the Investment Banking Exco at October 24 would have been aware of the August trading performance of the casino (at the very least).
134. A list of Aqua comparable companies on international exchanges is detailed on V13<sub>431</sub> highlighting the international demand for these types of investments and the relative pricing parameters.
135. In the latter half of 2000 a dispute arose between Corpcapital and Sean / Tal in relation to a bonus claimed by them. I deal with this in Appendix 6. The issue is relevant for the purpose of showing that there was an arm's length and often difficult relationship between Corpcapital and Sean / Tal. Sean and Tal were not nominees of Corpcapital or any of its executives. Corpcapital fought to enforce proper principals of corporate governance and process and was often met with resistance.
136. In September 2000, Deloitte & Touch produced a report highlighting internet valuations and comoarable bench mark criteria (V15<sub>4</sub>). This gave us an indication of industry pricing criteria at the time.
137. My Investment Banking Exco report dated 13th November 2000 (referred to Netainment results to September 2000 (V15<sub>75</sub>) I mentioned that the due diligence of both the English Harbour and Netainment businesses had been concluded satisfactory. It also mentioned that PKF (London) had been approached to audit Amalco.

J. HAMBURGER: STATEMENT

138. Revenues for the month of September increased 14% \$2.4m.
139. In December 2000 I noticed that Ladbrokes had begun to aggressively market its online casino in the English press, (refer V15 297.) This confirmed my thinking that the London market was becoming more receptive to this industry. In the past online casinos were not permitted to advertise in the UK through the traditional media (print, outdoor). *Today they advertise prolifically e.g. dominant advertisers of international sport (cricket, soccer) events,*
140. In January 2001 Merrill Lynch released its in-depth report on E-gambling (refer V16 <sup>63-215</sup>.) This report confirmed our thoughts on the industry at the time. In summary Merrill Lynch believed the online gaming market would demonstrate superior growth prospects and that internet gaming properties were very valuable. A summary of Merrill Lynch's E-gambling report is provided on V18<sub>169</sub>.
141. Merrill Lynch valued the Stanley Leisure and Ladbrokes online casinos businesses. Notwithstanding these casinos had less operating track record and profitability (they were in fact loss making) compared to Netainment (they were in fact loss making at the time of valuation), Merrill Lynch valued these businesses in excess of Corpcapital's Netainment valuation. Netainment was an identical business, trading in the same markets with a similar product offering (Ladbrokes operated off the MGS platform).
142. The material assumptions used by Merrill Lynch with respect to growth and discount rates were more aggressive than those applied in the Corpcapital valuation. Please refer the detailed "Cytech Valuation" document for further comparison to Merrill Lynch.
143. The Merrill Lynch report validated the approach, methodology and material industry assumptions used in the Corpcapital valuations.
144. In December 2000 Evan Hoff ("Evan") was identified as the potential CEO for Netainment. Sean, Tal and I believed that Evan was responsible for the success of VR Services. The MGS casinos established and managed by VR Services were industry leaders.
145. Evan was articulate, intelligent and a strategic thinker. He was hired in March 2001 on an expensive package after his restraint with MGS ended.
146. Between Sean, Evan and the (soon to be) newly appointed financial manager (Alex Astenga "Alex") a business that had previously operated with minimal infrastructure (due to its outsourced business model) was supported with senior personal as part of a comprehensive growth and diversification strategy.

## J. HAMBURGER: STATEMENT

147. When Evan joined I insisted on a strategic planning session, (held in South Africa on 28 March 2001) to align the Sean/Tal and Corpcapital's thinking with respect to the future of the business (and to give Evan a carefully articulated plan going forward). To facilitate a meaningful session I prepared a comprehensive strategy document outlining plans to form a diversified online gaming group that could take advantage of the growth opportunities in the industry (refer document on V17ss). This document sets out our views at the time and was the factual underpin for the February 2001 valuation. The key points are highlighted below:

147.1 Cytech was viewed as a cash cow (generating regular cash flow profits). It has no large capex needs. Shareholders could elect to receive regular dividends without impairing the business.

147.2 The business was growing exponentially.

147.3 The business had one product (the online casino) operating in an increasingly competitive market.

147.4 There was debate over whether barriers to entry were high or low. (Merrill Lynch in particular believed that the emergence of dominant online brands would create barriers to new entrants).

147.5 Merrill Lynch assumed that the marginal incremental cost of attracting a new player would cost less over time (therefore assuming that financial margins of the internet casino would increase). Notwithstanding this view of increased margins, Corpcapital and management were more conservative in its forecasting of future Netainment margins. (In the Feb 2001 valuation we forecast lower margins over time as a result of increased competition).

147.6 Merrill Lynch predicted super normal profits for the next ten years followed by a transition phase of five years up to industry maturation in year 15. (In the Feb 2001 valuation, we forecast business growth for 3 years followed by "maturation" represented by a terminal growth of 3%).

147.7 Merrill Lynch forecast that the complete prohibition of e-gambling in North America, if successful, would only reduce the total market size by 33%. Merrill Lynch do not expect this to happen and forecast some regulation (which was welcomed by Netainment) within the next four years. Given that Netainment's business at the time was approximately 50% outside of the US and growing, this threat was viewed as less important. Additionally, I felt that this made Netainment an attractive business relative to its peers.

## J. HAMBURGER: STATEMENT

148. The conclusion drawn by the strategy document was that Netainment should develop a multiple product strategy to leverage off the industry knowledge and skills of its management team and its existing customer base. This would reduce reliance on the online casino and create synergies to leverage across various other applications (cross marketing to each products' client base was particularly appealing).
149. The strategy document was circulated within Corpcapital (to Martin, Benji, Jeff and Mark Matisonn). It was considered to accurately reflect the views of Corpcapital at the time. The strategic initiatives proposed in this document were widely accepted as the way forward for the group to deliver on the growth opportunities. Evan was the champion to drive this strategy forward.
150. After the strategy session, Mark Matisonn prepared minutes and distributed them to Jeff, Martin and myself highlighting the growth strategy going forward (V17<sub>98</sub>28 March 2001). These minutes contained the following key points;
- 150.1 Netainment needed to diversify its product offering and leverage the customer base and management skills.
- 150.2 Sean and Evan believed that a listing at this time should not be pursued, given the current growth initiatives. Jeff disagreed saying that a listing would facilitate a consolidation or growth strategy.
- 150.3 The Digiturf shareholder's valued their company (a start-up virtual horse racing application) at between \$20m and \$30m. The initial Digiturf capital raising was at a pre-new-money value of approximately \$6m (based on the concept only). Jeff and I were highly conscious of over paying for a business that was currently in conceptual stage.
- 150.4 It was noted that Netainment had \$4.5m cash in the bank. A dividend of between \$1 and \$1.5m was proposed.
- 150.5 The opportunity for a VC fund to invest capital in the business at an appropriate value was discussed.
- 150.6 Evan discussed a potential merger opportunity with Anthony Moshal (the brother of Martin Moshal). Anthony's business was a comparable online casino using MGS software with revenues of \$4.5m per month and an estimated PBT of \$10m per annum.
- 150.7 Everyone was in agreement that the medium term Netainment strategy was to list.

J. HAMBURGER: STATEMENT

- 150.8 It was noted that Netainment was in the process of nearly doubling its staff compliment from 9 to 17 people.
- 150.9 Jeff agreed with the strategy but voiced his concerns at the time of the ability of the executive to execute and deliver timeously.
- 150.10 Sean and Evan were pushing for increased remuneration packages (both Evan and Sean were on effective salaries of over £100 000 per annum each).
- 150.11 The minutes reflect our insistence that the governance and internal control aspects of the Netainment group needed to be upgraded. Evan committed to focus on improving this. Evan additionally agreed to improve the process of shareholder communication (in respect of financial results, making new investments).
151. Although the strategy session was held after the formulation of the February 2002 valuation, the facts and circumstances contained within the strategy document (prepared by me) were known to me at the time of executing the indicative valuation.

**THE FEBRUARY 2001 VALUATION**

152. The February 2001 indicative valuation was performed and finalised in March 2001 (V19<sub>150</sub>).
153. A summary of the key business drivers of the indicative valuation at this date were:
- 153.1 Actual profits were ahead of forecasted profits.
  - 153.2 The business continued to grow.
  - 153.3 The trend continued to be very positive.
  - 153.4 Relevant industry analysis supported our valuation assumptions.
  - 153.5 A strategy to for future growth had been articulated
154. In February 2001 the fair value of the business was determined to be \$57.1m (100%) and \$27.1m (47,5%). Please refer to the "Cytech Valuation" document for further detail.

### THE EVENTS LEADING UP TO THE AUGUST 2001 VALUATION

155. Evan was supportive of the multi-product strategy and was determined to build an operational infrastructure in London to support the alternative gaming products.
156. The development and roll-out of the new gaming products consumed senior management time and utilised other company resources. The start-up nature and excitement of the new initiatives were distracting. Management lost sight of where the money was being made (the casino business). The casino was not necessarily neglected but definitely suffered as a result.
157. The multi-product strategy identified in the strategy document (V17<sub>3</sub>) ultimately developed (over time) as follows. The success or failure of this strategy was not fully appreciated until 2002.
- 157.1 The Casino:** Profitable new markets were successfully developed (Greece and Turkey). A new software platform was acquired.
- 157.2 Quiz:** A budget to develop an online Quiz application was approved (approximately \$500 000 funded by CFI initially). Evan secured additional finance from high net-worth individuals. A champion for the business was employed and Aqua developed the application. Unfortunately the product was not popular. Additionally the development of the application took longer than expected, was more expensive and failed to meet the technical objectives. It was evident that this product was a failure from the beginning (although Evan failed to see this). We refused to sanction any further investment). The business unit was ultimately closed down in March 2003.
- 157.3 Lottery:** A Swiss based online lottery was introduced to us. The business (Zabadoo) required a capital injection. Although the business was operational it was not making money. The deal terms proposed by us were rejected by the Lottery business. The deal was never concluded and I understand the Lottery subsequently went insolvent.
- 157.4 Greyhound Racing:** On 12 March 2001 Nic Frangos introduced Corpcapital (Jeff and I) to Nigel Robertson, an internet entrepreneur who had made considerable profit by selling Scoot.com (an online directory inquiry service company).

## J. HAMBURGER: STATEMENT

*Nigel was involved with Gaming Internet, an online casino and Greyhound racing betting business. The potential merger of Netainment and Gaming Internet was discussed in V11<sub>18</sub>. Gaming Internet's then market capitalization was in excess of \$50m (benchmarked by a private fund raising of \$8m). I discussed the relative value parameters to be used in a merger of Netainment and Gaming Internet with Nigel. Given his understanding of the current profitability of the Netainment business (and lack of substantial profits of his business) he acknowledged that Netainment would necessarily own more than 50% of an enlarged merged group. (This implied a value for Netainment in excess of \$50m).*

*Ultimately Evan and Scan dismissed the opportunity given the risk of the "start up", loss-making Greyhound division. A deal proposed by Nigel presumed that Netainment would only get half of the enlarged group was not attractive (even if it did fast-track a London listing). (Detail on Gaming Internet is provided on V17<sub>39 / 60</sub>.)*

157.5 **Virtual Horses:** *The opportunity to acquire Digiturf was never concluded given the price aspirations of the Digiturf vendors. The application has yet to take off (two years after our initial discussions) and I understand that the business is marginally loss making.*

157.6 **Bingo:** *A bingo application was developed by CFI. The product has recently been launched (in 2003) and early indications are that it is successful (Bingo has achieved a cash break-even position after 4 months of trading).*

157.7 **Overheads:** *Evan aggressively hired staff in London to support the strategy. New premises were leased and infrastructure invested in. Overheads almost doubled.*

158. In March 2001 the Bear Stearns flaming industry report was released (V17<sub>167</sub>). A summary of this report is provided on V17<sub>286</sub>.

158.1 Bear Stearns updated their opinion on the industry. In February 2000 they characterized the online gaming industry as having low barriers to entry.

158.2 Bear Stearns now concluded that barriers were rising in 2002. This favoured Netainment as I was of the view that increased barriers meant fewer competitors and improved margins. As a result, Netainment, given its critical mass, capital invested in infrastructure, significant client database and brand name would consolidate its position in the market. Undercapitalised new entrants would fail,

## J. HAMBURGER: STATEMENT

The industry would consolidate and the larger players, (like Netainment) would benefit.

- 158.3 Notwithstanding the concerns raised by Bear Stearns in this report, they still forecast compound annual growth rates to 2003 of 36.4% for online casinos.
- 1 58.4 Bear Stearns also forecast that new payment technologies would mitigate the risk of credit card legislation.
159. On April 6th 2001 my investment banking Exco report covered the results to February 2001. In this report I note the non-recurring executive "bonus" and legal fees (in respect of the English Harbour merger).
160. The May 2001 investment banking Exco report contained results to March 2001. This report included the following information:
- 160.1 The growth strategy adopted by Netainment that would result in the employment of more people in London.
- 1 60.2 In the Netainment results there was approximately \$50 000 of abnormal marketing expenditure relating to the once-off purchase of a car in support of an Israeli marketing initiative (V18<sub>36</sub>)
161. In May 2001 I proposed that a company valuation of approximately \$70m could be used for the purpose of determining executive options for Evan and Alex. I argued that the business could be worth \$60m - \$70m on the basis of 1 2 months forecast profits of \$6m -\$ 7m and a PE of 10x (using a recent Aspinals acquisition multiple as a benchmark). Given that a discount would be given to the staff the company valuation would range between \$40 and \$50m (V17<sub>304</sub> to <sub>305</sub>) for staff incentive purposes for the purposes of awarding options.
162. In my Exco report of June 2001, Netainment results to April 2001 were presented. I mentioned that approximately \$100000 was spent to establish the new office infrastructure. I note that April's profit was approximately \$230 000 which was a decrease of 40% from March (\$379 000) consistent. Evan had begun to significantly increase marketing expenditure without concomitant increases in revenue. Profits were less as a result of an inefficient marketing and abnormal infrastructure establishment costs. After removing the infrastructure set-up costs of \$100 000 profits were only 13% below the previous month on a like for like basis. Revenue was 4% ahead of March. I was unconcerned as I felt the decline was not indicative of a trend.

J. HAMBURGER: STATEMENT

*162.1 We did not adjust these infrastructure costs in our determination of sustainable profits for the purpose of the indicative valuations.*

163. In June 2001 an article in the LA-Times forecasted that Nevada land-based casinos would soon legally be entitled to migrate their businesses online. In a Benji memo dated 7th June 2001 to Martin, Dave Leibowitz and myself he confirmed our thinking that this an opportunity to become acquired by a Nevada operator who would require an instant entry into the market. Additionally Benji mentioned that this is good for the industry because it "undermines the basic argument that online gaming is illegal and unwanted" (V18<sub>9</sub>).
164. Evan maintained in June 2001 that a sustainable marketing efficiency for the business was 4x (marketing expense as a percentage of revenue equals 25%) (Refer V18<sub>15</sub>). Both Corpcapital's August 2001 and February 2002 valuations adopted more conservative marketing efficiency ratios.
165. KPMG tested my February 2001 valuation for reasonableness for the purposes of the Corpcapital group merger. KPMG's findings are contained in KPMG's report. These findings were updated by KPMG in August. (In August 2001 we would have been aware of June's results). Although I have no specific recollection of my conversations with KPMG I have no doubt that I relayed the following facts to KPMG as these facts were directly relevant to an update performed by them:
- 165.1 Revenue from February to April had increased. May had decreased but in relation to forecast in February this was not considered a trend as June was showing signs of growth;
- 165.2 Profits were volatile and had decreased but were affected by the abnormal infrastructure costs in support of the multi-product strategy ( $\pm$ \$100 000) and inefficient marketing campaigns assumed to be abnormal;
- 165.2.1 I was still confident that the growth strategy was going to be successful.
- 165.2.1.1 The credit card issue had not impacted the business yet but the software deal had been anticipated (I was aware by July that a deal was imminent and that this would improve the inherent value of the business)*
166. The Netainment financial manager Alex joined in July 2001 and I prepared a work program for him (V16<sub>28</sub>).

J. HAMBURGER: STATEMENT

167. Evan complained that the Aqua fees were not market related relative to the cost of performing the service. This confirmed the evidence of the relatively low administration overheads required to support the English Harbour business (evidenced during the due diligence).
168. In the July management pack Evan states that "much of the increase [of marketing spend] was unsuccessful due to the purchase of inefficient ad-buys". This implies that at a point there are diminishing returns from additional ad spend.
169. The London infrastructure costs were increasing rapidly. Evan justified the increase in overheads (V18<sub>35</sub>) as necessary to support the growth strategy.
170. In July, as a result of the June USA "credit card issue", I sent an email to Sean and Evan (dated 23 July 2001- V18<sub>37</sub>). The casinos' numbers had not been affected discernibly by this banking initiative (primarily at the time because not all the major banks had begun to block gaming transactions and because the business was not reliant solely on the US market). There were a number of facts and circumstances which in my view impacted positively on the prospects of the business as a result of the credit card issue. They were:
- 170.1 barriers to entry had significantly increased which could decrease competition.
  - 170.2 it would be more difficult for a customer to switch casinos (customer loyalty would increase).
  - 170.3 the larger sufficiently capitalized casinos would outperform smaller casinos that were expected to fall away or be consolidated.
  - 170.4 I believed that Microgaming's royalty fee was unsustainable in an environment of decreasing margins and they would ultimately agree to a reduction across the industry.
- I also stressed that the business should continue to focus on the following identified growth strategies:
- 170.5 Diversifying its customer base outside of America
  - 170.6 Identifying alternative payment mechanisms,
  - 170.7 Entrenching customer loyalty; and
  - 170.8 Considering a consolidation strategy to acquire smaller casinos.
171. In July 2001 I was convinced that the "credit card issue" was not an issue of substance.
172. By July 2001 discussions were underway with IMS regarding a change to the casino software used by Netainment (V18<sub>40</sub>).

J. HAMBURGER: STATEMENT

**New software**

173. The relationship with MGS had been strained for some time. Sean and Tal resented MGS's frustrating actions in respect of the English Harbour merger. Additionally Sean, Tal and Corpcapital believed that the MGS licence fee was uncompetitive (relative to the industry) and too expensive (relative to the alternative of building your own product).
174. Sean and Tal had built up a relationship with Jack Stroll, the operator of the Golden Palace online casino. Golden Palace was one of the first and larger online casinos in the world. Golden Palace was one of MGS's initial clients.
175. Jack had recently migrated his players onto a software platform that he had effectively developed in-house. Jack informed Sean and Tal that he was very pleased with the results of the migration and that he had lost very few of his player database during the move. Additionally, Jack mentioned that his business quickly returned to pre-changeover revenue levels (this indicated to us that the software was of equal quality to the MGS system)
176. Sean and Tal were very excited to hear of an alternative MGS product and began to discuss the opportunity to licence the software.
177. The negotiations culminated in the IMS/Cytech software license agreement that was concluded with effect from 1 October 2001 (V18<sub>187</sub>).
178. The key terms of the software agreement were largely agreed by September 7 2001 as follows:
- 178.1 A licence fee calculated at 7.5% with reference to revenue (after deducting promotional money and credit card charge-backs). *As MGS royalties were calculated with reference to revenues only, the equivalent effective royalty on the IMS software for comparative purposes (i.e. the IMS royalty calculated as a percentage of revenue alone) was approximately 6.75%;*
- 178.2 A minimum monthly royalty of \$100 000. *Cytech monthly revenues never consistently grew above the level (\$1.3m) required to avoid paying the minimum.*
179. The positive effect on the financial margins of the business as a result of this agreement are dealt with in detail in the 'Cytech Valuation' document.
180. Stanley Leisure released its results and I considered approaching them for a trade sale in July 2001.

## J. HAMBURGER: STATEMENT

181. In the July management pack Evan says "much of the increase. [of marketing spend] was unsuccessful due to the purchase of inefficient ad-buys"
182. In an email from me to Martin dated 12 June 2001 (V18<sub>55</sub>) I mentioned that Netainment had approximately \$5m in free cash. I proposed distributing this to shareholders and then raising new money from outside shareholders at a pre-new-money valuation of \$60m. At the time Corpcapital was considering creating an 'investors club' of high net-worth individuals who were considered potential investors in opportunities Corpcapital presented them. This proposal was not progressed, as it was considered unlikely that the investors would invest debt funding into the business.
183. In September 2001, RedHerring published an article detailing the average PE ratio on a basket of 1000 domestic and foreign technology companies. The average PE ratio was 26x 2002 earnings (a forward multiple). Additionally RedHerring expected earnings for technology companies in the S & P 500 to increase by an average of 55% in 2002.

184. In September 2001:

184.1 Stanley Leisure, Sportingbet and MGM Mirage were believed to be the 3 casino groups awarded licences to operate in the British Isles;

184.2 Sun International announced that they had been awarded one of three gaming licences by the Isle of Man to operate an online casino (V18323). *This was interesting as Kevin Joselowitz had a good working relationship with Sun International. I believed that in the medium term they could be approached as a potential trade buyer of Netainment.*

These developments reinforced our thinking that the UK market was the most receptive jurisdictions to online gaming businesses.

155. In September 2001 (after the September 11th events) Nomura pitched to Aqua to assist in Aqua's London listing. Nomura's view on the then current market conditions was that notwithstanding the fall in technology indices worldwide, the AIM market had proved extremely resilient. They further noted that a shift in sentiment towards the technology sector may be occurring and that Aqua's track record and profitability should provide a good platform from which to approach the market. They were confident that Aqua could raise between £3-5m within the following six months (V18<sub>144</sub>).

J. HAMBURGER: STATEMENT

**New Aqua contract**

186. Aqua and Netainment entered into a new administration services contract with effect from 1 October 2001. The commercial terms of this contract were negotiated well in advance of October 2001 (V18<sub>174</sub>). The August 2001 valuation forecasts therefore included reference to the reduction of this expense. The terms of this contract included:

186.1 A reduced administration fee calculated at 7.5% of Cytech revenue.

186.2 The purchase of the Aqua / Kings Solomon marketing team from Aqua at a capital cost of \$600 000 payable in twelve equal instalments of \$50k per month. .

J. HAMBURGER: STATEMENT

**THE AUGUST 2001 VALUATION**

187. The preliminary Netainment audited results for the 36 months ended 30th September 2001 were presented to Corpcapital in or around September / October 2001 (V18<sub>244</sub>). As expected, these results reconciled to the management accounts that we had been reviewing, giving us further comfort on financial results for the purpose of the August 2001 valuation.
188. I was confident that that the prospects for the business leading up to the August 2001 valuation were attractive based on the following:
- 188.1 Alternative growth strategies were identified during the strategy session.
  - 188.2 Evan was a new CEO with relevant industry experience to assist in the implementation of the growth strategy.
  - 188.3 The business was investing capital in new infrastructure to fund the growth.
  - 188.4 New software was identified.
  - 188.5 Aqua contract had been renegotiated.
189. The August 2001 valuation was finalised in September 2001 [V18<sub>147</sub>]
190. A summary of the key business drivers of the indicative valuation at this date were:
- 190.1 Revenue was forecast to be 19% less than the prior years actual revenue.
  - 190.2 In August and September there was an international reduction of turnover.
  - 190.3 The credit card issue had not yet affected the business materially.
  - 190.4 The reduction software royalty and Aqua fee were forecast to significantly increase margins.
  - 190.5 This was a margin driven valuation. We held the view that the business would be more profitable off a lower turnover (due to variable expense savings).
191. In August 2001 the fair value of the business was determined to be \$55.4m (100%) and \$26,3 (47,5%). Please refer to the "Cytech Valuation" document for further detail.

**Events around the time of the finalisation of the August 2001 valuation;**

192. Soon after the software switchover Netainment management indicated that the player acceptance of the new software had been very good (V18 263). This view was supported in the following email correspondence:
- 192.1 12<sup>th</sup> October 2001 -Evan stated that every day since the changeover had resulted in an increase in player purchases. (V18 237)
- 192.2 On 22nd October 2001 -Sean enthusiastically reported that the previous weekends' total player purchases was \$324 000 verses a typical Microgaming weekend of \$320 000 (V18<sub>263</sub>).
193. By the time of the release of Corpcapital's August results in [October 2001] the initial indications were that the casino migration had occurred successfully and the business was on-track to meet forecasts.
194. The actual revenue and profit earned for the months of September and October approximated forecast (if you remove the abnormal promotional expense relating to the migration-refer "Netainment Valuation"). I would not have had the actual results for October before the release of Corpcapital financial statements. Detailed below is an review of the forecast and actual revenues and profits immediately post year-end. As results approximated forecast there would have been no need to consider changing the fair value for the purpose of releasing the Corpcapital financial statements.

Netainment results versus forecast		
Revenue (\$'000)	Sept 01	Oct 01
Forecast at August 2001	1969	1750
Actual	1885	1750
Profit (\$'000)	Sept 01	Oct 01
Forecast at August 2001	379	250
Actual	434	88*

- Note: \* Promotional spend of ± \$700000 in October compares to a normal month of \$150000

J. HAMBURGER: STATEMENT

**THE EVENTS LEADING UP TO THE FEBRUARY 2002 VALUATION**

195. Gaming Insight's results (formally Gaming Internet) were released Friday 28th September 2001. Turnover was up 351% driven by a major contribution from Zap Casino (its online casino division). Gross profit was up 365%. The release was complimentary of the online casino's growth and success. (V18<sub>136</sub>), reinforcing our positive perspective of Netainment.
196. Netainment sold its business (excluding the MGS contract) to Cytech for shares in Cytech with effect from 1 October 2001 (Please refer Kevin Joselowitz's document for the rationale behind the disposal). Subsequently, Cytech became a wholly owned subsidiary of Netainment.
197. The Columbus Casino brand was launched in October 2001 and in its first month contributed revenue of \$26 000. Management believed that alternative casino brands (the business now operated 3 brands) would support growth initiatives.
198. A further strategy session was held on 5th November (refer agenda-V18<sub>267</sub> and the strategic plan-V 18<sub>273</sub>).
- 198.1 The minutes of the strategy session (V18<sub>284</sub>) noted that that given the recent change in software, the executive management of Cytech should be focused on driving turnover.
- 198.2 Evan strongly felt that the diversified product strategy should continue.
- 198.3 The executive management agreed to focus on strategies to deliver casino turnover of between \$2m - \$2.5m per month.
- 198.4 The minutes reconfirmed the strategy to pursue non-US markets.
- 198.5 A budget of \$200000 was approved to pursue the alternative growth markets identified in Korea and Taiwan.
- 198.6 Turkey was also considered a potential growth opportunity (*by September 2003, Turkey was the third largest Cytech market after Israel and Greece*).
- 198.6.1 *The revenue growth forecast used for the purpose of the February 2002 valuation assumed that \$2.5m revenue per month would only be reached by November/December 2002 (one year after the software change).*

## J. HAMBURGER: STATEMENT

- 198.7 The strategy session identified a range of software enhancements that IMS would be required to implement.
- 198.7.1 *The business realised close to a year after the changeover that IMS were not geared to service the business adequately. Numerous requests went unanswered. The affiliate system application was delayed for two years and implementation of new payment switches were always delayed. This severely undermined the performance of the new software and frustrated strategic initiatives to the detriment of the business. This subtlety was not comprehended fully until calendar year 2003.*
199. In my investment banking Exco report of November 2001 I commented on results to September 2001 (V18 13). I mentioned the following:
- 199.1 Marketing was reduced in September 2001 in anticipation of the change in software and player migration in October.
- 199.2 September's high marketing efficiency resulted in the month's large profit. I noted that September's marketing efficiency was not sustainable.
- 199.3 Management was focused on growing the revenue to \$2m in the short to medium term (by March 2002). This was to be achieved by exploiting the database and focusing on the US market. After achieving the \$2m level, Netainment would continue to pursue its multi-location strategy (Korea and Taiwan).
- 199.3.1 *The February 2002 valuation forecast assumed revenue to reach \$2m by May 2002*
- 199.4 Millions -2-win had been launched and management expected this marketing portal to drive revenue growth.
200. In November 2001 Arena Leisure (a diversified race course and media group) was reported to be making a bid to acquire Gaming Insight (Nigel Robertson's company). Insight had a market capitalisation of £30m but Nigel demanded a premium to the then current share price. From our previous discussions with Nigel Robertson we (Netainment) concluded that our business was more profitable (and therefore more valuable) than Gaming Internet (as it was called at the time).
201. Interactive Gaming News (an industry publication) surveyed its readers to see the effect of the credit issue on its reader's business revenues (November 2001). 37% responded that

## J. HAMBURGER: STATEMENT

revenues were not affected. 18% of company's revenues were down by less than 25%.  
(V18<sub>292</sub>).

- 201.1 At this time the online casino industry was predominantly focused in the US market.
- 201.2 Some of the major US banks (like CitiBank) only began to regulate gaming transaction one year after the initial wave of banks (in June 2002).
- 201.3 Approximately half of the Netainment business in November 2002 was focused outside of America and these players would not have been affected by the credit card issue to the same extent as the US players.
202. I was requested to prepare a valuation presentation to the Corpcapital board. The presentation was scheduled for 26th November 2001 (V18 305). Although I was available at the allotted time (I was waiting outside the boardroom) I was never called to do the presentation.
  - 202.1 I noted in the presentation that the new software had received a very satisfactory acceptance by the old players. Approximately 50% of the casino's VIP's and 30% of entire database had migrated.
  - 202.2 I also noted that we were tracking forecasts to the end of October 2001. I explained that June 2001 revenue (prior to the US rejection of credit card purchases) was forecast to be achieved in October 2002.
203. The business was tracking ahead of expectations at this time. I believed that forecast profits would exceed budget because marketing was being curtailed to focus on short term profitability. Additionally I forecasted that operations would be moved to Johannesburg to take advantage of the lower cost of South African infrastructure. At the time I noted that there were preliminary discussions with Golden Palace to merge operations and leverage off the planned Golden Palace London listing in the first half of calendar year 2002.
204. In January 2002 a meeting was held in London between Jeff, Sean, Tal and myself where the following points were discussed (Refer V16 2).
  - 204.1 The growth of the business should be more conservative as the shareholders wanted to manage the business for cash dividends.
  - 204.2 A dividend payout of 50% of quarterly earnings was agreed.
  - 204.3 Evan's strategy to "buy market share" and aggressively target top line growth was not working. At the time we discussed the replacement of Evan and Alex and the relocation of the infrastructure to South Africa.

## J. HAMBURGER: STATEMENT

- 204.4 Aqua was considering delisting and we discussed whether Netainment would be considered a potential buyer of the Aqua Gaming business.
- 204.5 Corpcapital needed to develop a closer working relationship with Jack Stroll of Golden Palace (Tal and Sean mentioned that Jack was considering a London listing and that we should consider merging with Golden Palace pre-listing).
205. Jeff and I met Jack Stroll on 25th January 2002 with Sean and Tal in London.
- 205.1 It was evident that Jack held Sean and Tal in the highest regard.
- 205.2 Jack seemed interested in the low cost -infrastructure of our operations in South Africa.
- 205.3 Jack intimated that he would be listing in the first half of 2002 in London.
- 205.4 He seemed keen to merge operations in anticipation of his listing.
- 205.5 He agreed that the London market would prefer an enlarged group with low cost infrastructure.
- 205.6 Sean and Tal had discussed merger opportunities with Jack previously. This meeting confirmed Golden Palace's preliminary interest in a Cytech deal. We resolved to discuss the potential merger over the next few months.
206. In January 2002, a Cryptologic brokers note contained the following information relevant to our February 2002 market outlook (V19<sub>4-7</sub>):
- 206.1 Cryptologic's further quarter results fell below expectations as a result of the credit card rejections, high jackpot win rate and low levels of play.
- 206.2 Notwithstanding this, Cryptologic indicated that first quarter results would still grow by 30% and 20% in respect of revenue and earning targets respectively.
- 206.3 Cryptologic mentioned that its licensees were utilising additional payment options like bank wires, electronic cheques and PayPal to neutralise the credit card issue. .
- 206.4 Cryptologic's forward earning's multiple was 10.7 times.
207. A Boss Media analysis report dated 4 February 2002 (V19u) (received by us in or around February / March 2002) on was broadly negative and implied that the credit card issue was affecting business considerably. Even so EV/Ebita multiples were still high at 19 times forecast earnings.
208. In my 14 January 2002 Exco report I mentioned the following

## J. HAMBURGER: STATEMENT

- 208.1 November's revenue (after deducting promotional expenses) had increased 42% on October (this was exaggerated by October's comparative number being effected by the substantial promotions granted to migrate users onto the new platform).
- 208.2 Turnover growth reflected the success of the new software.
- 208.3 Early indications were that the software had been successfully implemented.
- 208.4 The technical aspect of the migration was successful and initial player comments were positive.
- 208.5 Average purchases per player during November were \$687 against October of \$584. November's average player purchases approximated the average for July and August 2002. This indicated that players were becoming more comfortable with the software (V18<sub>289</sub>).
- 208.6 Management were about to enter new countries (Portugal, Korea and Taiwan). This was thought to be a key driver of future growth.
209. In January 2001 Jeff and I met PwC Corporate Finance (London). In a discussion with the partner responsible for gaming we are given an indication of the indicative industry multiples attributable to an online casino. Ebitda multiples were quoted on a sustainable profit of between 8-1 Ox for non-USA earnings, and 2-4x USA profits.
- 209.1 PwC Corporate Finance represented that they had online casino experience.
- 209.2 PwC (London) was mandated to sell Cytech.
- 209.3 I received an engagement letter from PWC on 26th February 2002 (V19<sub>32</sub>) that was signed in early March 2002.
- 209.4 The fee quoted by PWC began at 1.5% of the transaction value up to £25m, increasing by 3% on the next £10m of value, and by 5% on the remainder over £35m.
- 209.5 PwC believed that UK listed companies like Ladbrokes, Gala and Paddy Power could be interested in our online casino given the predominance of non-US players.
- 209.6 *The PWC (London) information memorandum was distributed to the potential purchasers in May 2002 (post finalisation of the Feb 2002 valuation)*
210. In February 2002 a BBC news report indicated that Internet gambling was still showing signs of growth. A quote from a media research survey performed by Jupiter Media Matrix mentioned that December 2001 visitors to online gambling websites was up significantly

## J. HAMBURGER: STATEMENT

From the previous year. KSCasino.com (the Cytech website address) was mentioned in this article.

211. My March Investment Bank Exco report, commenting on January 2002 Cytech results (V19u5) contained the following comments:

211.1 A decision was taken to focus on profitability and reduce marketing expenditure.

211.2 Evan's forecast for February earnings was approximately \$380 000. This was determined with reference to the anticipated revenue for February and an estimate of February's budgeted marketing expenditure and the monthly overheads.

211.2.1 *The February 2002 indicative valuation contained a forecast profit for February 2002 of \$289 000. At the time of performing our February 2002 forecasts we believed that profitability would be increasing given this February forecast from Evan (refer January's Cytech management accounts).*

## HAMBURGER: STATEMENT

### THE FEBRUARY 2002 VALUATION

212. We were confident that the forecasts were achievable at the time of the February valuation because we believed the new software would still prove to be as popular as Microgaming but at a much lower cost. Additionally, we were confident that the growth strategies were still relevant (affiliate; portals, new markets for revenue growth and reduction in overheads given the move to South Africa).
- 212.1 Management understood that the Golden Palace migration was successful and that they had recovered to pre-switch over revenues (in a very short time).
- 212.2 June 2001 revenues (prior to US rejection credit card purchases) were only forecast to be achieved again in May 2003.
213. The February 2002 draft indicative valuation narrative contained a typing mistake. Forecast revenue detailed in the table on page 11 incorrectly referred to forecast purchases (which are approximately twice forecast revenue) for the years ending 2003, 2004, 2005. The excel spreadsheet (containing the financial model) attached to this report reported the correct position. This indicated a forecast estimate of flat turnover.
214. A first draft of the Cytech February 2002 indicative valuation was prepared on 22nd February 2002 for internal discussion (V1039). Cytech was valued at \$51,7m in this initial version. An internal debate and discussion occurred between Martin, Shane, Mark, Jeff, Tom Wixley (JH to check) and me. This internal debate considered an indicative value that was much lower than my first draft indicative value.
215. Following numerous further discussions the board approved a fair value of \$40,7m for Cytech (a decrease of 27% in dollars to the August 2001 Fair Value).
216. A summary of the key business drivers of the indicative valuation at this date were:
- 216.1 Initial indications were that the new software was well accepted by players;
- 216.2 Monthly revenue was only going to return to June 2001 levels (credit card issue start date) in May 2003.
- 216.3 Forecasted revenue was slightly less than the prior years actual revenue.
217. In February 2002 the fair value of the business was determined to be \$40.7m (100%) and \$19,3 (47,5%). Please refer to the "Cytech Valuation" document for further detail.

J. HAMBURGER: STATEMENT

**THE EVENTS LEADING UP TO THE AUGUST 2002 VALUATION**

218. In late March 2002 Sean entered informal acquisition discussions with Sportingbet. These discussions were not progressed as the Cytech shareholders believed that the initial indications of pricing by Sportingbet were below expectations.
219. My April investment-banking report detailed February 2002 results (V19<sub>87</sub>). I noted the following:
- 219.1 Revenue and profits were significantly behind budget.
  - 219.2 Infrastructure was relocating to South Africa and the business intended to scale down infrastructure in London.
220. A Sunday 7th April 2002 article in the London Observer gave an insight into the industry at the time.
- 220.1 Barriers to entry seemed to have risen dramatically;
  - 220.2 Online Gaming operators like MGM were moving online;
  - 220.3 The strategy for a successful online casino was determined to be a global, multi-currency, multi-product operation that could exploit economies of scale (this was Cytech's strategy in 2001).
221. A Business Week article dated April 29th 2002 (V19<sub>129</sub>) contained the following insight:
- 221.1 European online betting would grow from \$3.5 billion in 2002 to \$15.5 billion in 2005 (over 140% per annum).
  - 221.2 Merrill Lynch believed that Europe "offer[ed] the best environment for online gaming companies in the world".
  - 221.3 Entrepreneurs would find ways around the credit card issue.
222. Ladbrokes and Paddy Power showed initial interest in the Cytech business as a result of PwC (London) initiatives at company valuations approximating \$20m. These discussions never progressed past a preliminary stage.
223. In a June 28th 2002 article (V19<sub>198</sub>) experts believed that alternative systems to credit cards (like debit cards, smart cards and PayPal) would overcome the credit card issues.

## J. HAMBURGER: STATEMENT

The Bear Stearn's gaming analysts forecast that industry revenues in 2003 could drop by 16% from 2002 revenues.

224. The value of the business was ultimately undermined by the following factors:

224.1 The multi-product growth strategy that has not been successful yet. The Quiz initiative failed and the increased overhead was not required to support other products. (*Bingo looks to be an early success though*).

224.2 The systemic industry issues (credit card issue which began in June but which did not affect the business until the second quarter of 2002).

224.3 The software migration in October 2001 that proved a mistake as the software is of a lesser quality to the MGS software;

224.4 Evan was a disappointment (overheads increased without a concomitant growth in turnover or profits).

225. In August 2002 I formally proposed (to Corpcapital) a strategy to delist Aqua. If Cytech purchased Aqua, as contemplated, the Cytech consolidated profit would consist of the actual cost to administer the back-office support function.

**THE AUGUST 2002 VALUATION**

- 226. PwC (Jhb) were engaged to perform an independent valuation of the business.
- 227. A summary of the key business drivers of the indicative valuation at this date were:
  - 227.1 PwC carried out an independent valuation.
  - 227.2 Management's indicative valuation was within the PwC Range.
  - 227.3 The fair value was significantly lower than the February 2002 value.
- 228. In August 2002 the fair value of the business was determined to be \$21.8m (100%) and \$10,4m (47,5%). Please refer to the "Cytech Valuation" document for further detail.

J. HAMBURGER: STATEMENT

## APPENDIX 1: CORPCAPITAL INTERNAL PROCESS

### The management of the investment

1. Since inception I received monthly accounts from Netainment and CFI together with commentary. Initially I had telephonic discussions with Sean, Tal and / or the incumbent financial Manager about the results so that I could get a proper understanding of operating performance. These monthly interactions developed over time into fully-fledged and minuted monthly Manco meetings attended by me (and later with Mark Matisonn after he joined Corpcapital in January 2001). Subsequent to these monthly discussions with management I prepared a summary that would be included in the investment banking Exco report. Corpcapital executive directors attended the monthly Exco meetings.
2. Corpcapital required regular feedback on the performance of its investments. Our style of investment management was very "hands on". We were active shareholders. This was consistent with our rights in terms of the GA Agreement. Additionally, Corpcapital was involved in all the material corporate and operational decisions of the business (although we would rely on the operational management's representations before making a decision).
3. I began to report on the progress of our interest in Netainment to the Corpcapital investment committee as early as November 98. In a memo to me dated 18 November 1998 (V8<sub>202</sub>) Benji suggested, that Sean and Tal prepare written update reports to be circulated to Corpcapital. They subsequently complied (V8<sub>81</sub>).
4. I reported primarily to Jeff on a regular basis, updating him on the operational performance of the business and discussing corporate strategy. I often interacted with Martin, Benji or Shane when appropriate.
5. I frequently travelled to London to either monitor the performance of the Netainment operations directly or develop various corporate strategies relevant at the time (London listings, trade sales, acquisitions). I was in London each month from April 2000 to January 2002 (with the exclusion only of June 2001 and October 2001).
6. Information was relayed to Corpcapital executives members through a process of interoffice memos, specific issue meetings, e-mail, undisclosed meetings and general "corridor chats" and open debates in the canteen. Additionally, key issues and difficulties were

## J. HAMBURGER: STATEMENT

debated at length in weekly internal Investment Banking driven operational meetings and monthly Investment Banking Exco meetings attended by executive directors. Notwithstanding that a project team would have had intimate knowledge of issues at the time, the broader investment banking, Corporate Finance and Corpcapital executive members would have had at an understanding of key operational issues and each significant development.

7. On a monthly basis I reported to the Investment Banking Exco (attended by executive directors) on the performance of Netainment and the relevant corporate initiatives. On a weekly basis the Investment Banking team updated each other on the developments of each investment in an operational meeting (Opco). The Opco provided guidance on operational matters with respect to each investment. The Exco debated issues and guided my strategy with regard to the management of the asset. Additionally I received instructions from the Exco on administrative matters including the need for an audit of the investment, external valuations and process for communicating internal valuations.
8. The Corpcapital culture was "open door" and the management structure was very flat. This facilitated the free flow of information amongst executives (*except for Corporate Finance related matters with external third party clients*). Members of the Corpcapital executive and Investment Banking team had a good understanding of what was going on in the investments.

**APPENDIX 2: PROCESS FOR VALUATION PURPOSES**

**Valuation process for the August 2000 financial accounts.**

1. I prepared a detailed valuation model in Excel and a narrative of the key issues concerning the business incorporating macro industry factors, specific company initiatives a swot analysis, a summary of alternative valuation methodologies and a range of indicative values. The Excel model and narrative together constituted my indicative valuation. Shane Kidd reviewed the model in August 2000. His review included a review of the DCF calculations, the DCF assumptions and the forecasts. The model was debated with Shane in a series of discussions. I made changes to the model as a result of the discussions.
2. Once Shane and I were satisfied with the model it was sent to various executive directors (including Martin, Benji and Jeff) for their input and review. The review by the executive was comprehensive.
3. The model was subsequently given to FH for the purpose of their annual audit. FH audited the valuation as part of their annual audit of Corpcapital. This process included testing of the DCF calculations, review of the forecasts and audit verification of certain historical financial transactions and balances of Netainment.

**Valuation process for accounting periods subsequent to August 2000**

4. Mark Matisonn prepared the detailed valuation models and narrative on the same basis as above.
5. I reviewed the model on the same basis as above. The reviewed model was sent to various group executives for their input and comment (including Shane, Benji, Martin and Jeff).
6. The model was discussed with Mark and I at a series of internal review meetings.

## J. HAMBURGER: STATEMENT

### Valuation methodology

*The methodology as detailed below was consistently applied for reporting periods August 2000 - February 2002. In August 2002 PWC (Johannesburg) performed a valuation on their own basis to assist the board in determining fair value.*

1. Indicative Valuation prepared by Jade Hamburger, assisted by Mark Matisonn (primarily) for discussion with senior management and auditors in preparation for decision on Fair Value.
2. Indicative valuation was prepared using a Discounted Cash Flow ("DCF") valuation model by discounting three years of forecast earnings and a terminal value calculated using Gordon's Growth Model. Forecasts were prepared using historic sustainable earnings (excluding non-recurring expenses) as a base. Profits were assumed to approximate cash flows on the assumption that capital expenditure would approximate depreciation and working capital would be neutral. These assumptions were based on historic performance and the nature of the business. The valuations incorporated the assumptions that market participants would use in their estimates of fair value.
3. Forecasts for a period of three years were compiled taking into account reasonable estimates using industry background, operational issues, analyst reports, historical performance and operational management input. Relevant future operational initiatives were incorporated in the forecasts at the valuation date if management felt there was a strong likelihood of the events occurring.
4. Forecasts were prepared in US dollars. The forecast depreciation of the rand:dollar exchange rate was not taken into account. The terminal value was calculated using a 5% growth rate in August 2000 and a 3% growth rate thereafter. The terminal growth assumption is based on a long-term inflation assumption for the US. US inflation over the last 18 years has averaged 3%
5. The discount rate ("WACC") used was conservatively comparable to the prevailing rate of returns for financial investments bearing substantially the same characteristics and was calculated using the Capital Asset Pricing Model for a dollar income stream.
6. WACC of 24% used for all reporting periods.

## J. HAMBURGER: STATEMENT

Example of the assumptions used in the August 2000 valuation.

Risk free rate:	6.0%	10 years US Gov't bond yield (August 2000]
Market risk premium:	4.5%	Historic English market risk premium
Debt:	0.0%	
Beta:	2.0	Average Beta of companies listed on the IT sector of the JSE was 1,85 (August 2000). Stanley Leisure's (UK listed industry comparable) beta was 1,6.
Additional risk Premium:	9.0%	Further premium applied

The additional risk premium was intended to take into account the risk in forecasting a relatively young business in a dynamic, developing industry. The premium is considered relatively high compared to other valuations prepared for comparable businesses. Merrill Lynch in their valuations of online casinos used a WACC of 14.5% and CSFB in their valuation of Stanley Leisure used a WACC of 7.6%.

(During the period under review the 10-year US government bond yield reduced as a result of the declining interest rate environment. However the WACC was not reduced in the interests of consistency and conservatism.)

Turnover and earnings based valuations were also calculated as part of the Indicative Valuation with reference to the current market value of other instruments that were substantially the same. A range of values was calculated after performing sensitivity analysis on the respective earnings and revenue bases.

The DCF valuation was compared for reasonableness to these turnover and earnings valuations.

At each valuation date there were active markets where equity interests in online gaming operations were traded and from which, independently of the company itself and its management, information regarding operating trends (revenue) could be extracted. Corporate activities relevant to the company were also considered. After every valuation date regard was had to these active markets to verify assumptions, forecasts and valuations for reasonableness.

10. Senior management and directors of Corpcapital reviewed the Indicative Valuations. Based on the Indicative Valuation, numerous informal debates, auditors and audit committee inputs a value for reporting purposes was recommended for inclusion in the financial statements, which were then approved by the board of directors.

## J. HAMBURGER: STATEMENT

### APPENDIX 3: AUDIT INITIATIVES

1. Netainment is a Netherlands Antilles company and is not required by statute to produce audited accounts. Sean and Tal therefore felt no need to produce audited accounts.
2. I nevertheless exerted pressure on Sean and Tal to prepare audited accounts from early 2000.
3. The audit of Netainment was essential for the purpose of finalising Corpcapital's own audited accounts.
4. I was instructed by the Corpcapital Exco to have Netainment audited. As early as July 2000 there is evidence Shane reminding me to have an audit or review of Netainment's results to support the August 2000 valuation. He stressed that timing was critical as the work needed to be complete by the 22<sup>nd</sup> of September 2000 (V 12<sub>217</sub>).  
  
Shane constantly followed up on the status of the Netainment audit process (V13<sub>82</sub>) and I continued to pressure Sean and Tal to assist me [V13<sub>50</sub>].
5. At the time of the Amalco negotiations the parties indicated their intentions to list Amalco on the London alternative exchange ("AIM") within a year of the deal became effective.
6. Netainment (Sean/Tal and me) and English Harbour (Paul Sudolski) had preliminary discussions with two sponsoring brokers in London (Investec and Insinger) with regard to the AIM listing (in July 2000). We were advised by Insinger that the accounts of English Harbour and Netainment would need to be audited for the purpose of the AIM listing. This work was the responsibility of the Nomad (nominated advisor to the listing). All parties preferred a "big four" auditing firm to add credibility to the London listing.
7. When it became apparent to Corpcapital that the books of accounts of Netainment would not be in a position to be audited timeously, an alternative approach was discussed with FHS. FHS agreed that they could derive sufficient comfort on the Netainment results in August 2000 from a comprehensive review undertaken by its staff on the financial performance of the business.
8. I approached PwC (Johannesburg) (V13<sub>349</sub>) to get them to perform the necessary audit work. They advise that the London office is best suited particularly if a London listing is required. They offered to help liase with their UK office. I prepared a detailed response to some initial issues highlighted by PwC (Jhb) - V13<sub>364</sub>. The issues were principally around

## J. HAMBURGER: STATEMENT

- PwC gaining familiarity with the stakeholders and operators. I disclosed that Sean and Tal are beneficial 47.5% shareholders in the business (refer V1ei). Although initially keen, PW (London) could not get approval from its international compliance department.
9. PKF were simultaneously approached by me to perform the audit from London (V13<sub>427</sub>; V15<sub>107</sub>; V15<sub>158</sub>) (refer correspondence with Rhodri Whitoch where I disclose Sean and Tal's beneficial shareholding in Netainment (V15i6s). PKF subsequently confirmed that they would audit the Netainment business (V15<sub>313</sub>).
  10. Sean and Tal were reluctant to incur the expense of an audit for the September 2000 year-end if this cost was going to be repeated for the purpose of the Amalco listing - which was believed to be imminent
  11. In a memo to the English Harbour merger project management team dated 4 September 2000 (V13<sub>346</sub>) I reiterated the urgency to have the accounts of Netainment audited. I stressed that irrespective of the English Harbour merger Corpcapital required for its own audit purposes the accounts of its investments to be audited. Unfortunately there was no sense of urgency from Sean, Tal or the financial management team at Netainment to have the accounts ready for an audit. Refer audit email correspondence V13<sub>347</sub>.
  12. Paul Sudolski also began to exert pressure to appoint an audit firm for Amalco (V13<sub>373</sub>)
  13. Fisher Hoffman (Johannesburg) ("FH") was engaged to perform a review of the, Netainment financials sufficient to give them comfort for the purpose of Corpcapital's audit requirements in August 2000.
  14. Further correspondence between Shane and I regarding the Fisher Hoffman audit (September 19 2000) - Shane notes that we are running out of time. (V13<sub>385</sub>).
  15. I asked Shane to pressure Fisher Hoffman to perform the work timeously (V13<sub>392</sub>) -September 21<sup>st</sup>. I acknowledge that the auditor's work was a priority given the time constraints.
  16. In December 2000 I wrote to Sean and Paul informing them that PKF would perform the audit and that their respective financial managers should now manage the process.
  17. The Amalco merger was terminated (because of MGS). As a result, the benefits of engaging a London based auditing firm were outweighed by the costs. The AIM listing was shelved and FH (Jhb) were engaged to perform the audit of Netainment for the period ended September 2001.
  18. Detailed below is my summary of the work performed by FH on the Netainment results for the purpose of the Corpcapital year-end audit:

J. HAMBURGER: STATEMENT

19. Corpcapital's financial year ended 31 August 2000.

19.1 The auditors agreed historic revenue and material cost items in the Netainment income statement to external sources. They performed sufficient work to satisfy themselves that the Netainment management accounts results could be relied on for the purpose of determining the sustainable income base which was subsequently used in the Netainment valuation by Corpcapital.

19.2 During the period ended 31 August 2000, Netainment outsourced the majority of its operations to third party service providers. As a result, the majority of Netainment's revenue and expense items were traced to third party invoices. Consequently, the auditors could rely on the Netainment income statement after performing their audit review.

19.3 Detailed below is an example of Netainment's August 2000 month's results and an example of suggested audit procedures to illustrate this point. By vouching seven income statement items to the external invoices, the auditors could agree 80% of the income statement to third party documentation.

	Example month Aug-00 USD	Potential audit testing
Turnover / Drop	2,058	Agreement to 3 <sup>rd</sup> party casino software, royalty invoices, analytical review (x12)
Expenses Non controllable		
Royalty	451	Agreement to 3 <sup>rd</sup> party invoices and Analytical review (x12)
Aqua / admin	257	Agreement to 3 <sup>rd</sup> party invoices and Analytical review (x12)
Jackpot provision	147	Agreement to 3 <sup>rd</sup> party invoices and Analytical review (x12)
Transaction Processing	<u>234</u>	Agreement to 3 <sup>rd</sup> party invoices and Analytical review (x12)
	969	
Controllable		Sample and agree to 3 <sup>rd</sup> party Marketing invoices
Marketing Aqua media Placement fee (7.5% of mktg)	29	Agreement to 3 <sup>rd</sup> party invoices and Analytical review
Bad debts accrual 3%	62	Review of actual to accrual (historically Actual accrual)
Overheads	<u>37</u>	Some vouching of invoices
	462	

## HAMBURGER: STATEMENT

### 1. Corpcapital's financial year ended 31 August 2001

- The Fisher Hoffman engagement letter is contained on V18 126.
- The auditors performed an audit in accordance with South African Aud'ing Standards ("SAAS") of Netainment's historic financial information.
- Auditors issued draft financial statements (prior to the sign off of Corpcapital's Netainment valuation). There were outstanding items that required follow up but were subsequently resolved without affecting revenue or earnings.
- In February 2002, the auditors presented final audit accounts for the period ending September 2001 for sign off by the corporate directors. No material discrepancies with the management accounts were identified.
- The responsibility for implementation of the audit and statutory requirements of the foreign subsidiaries of Corpcapital was given to Ruth Credo (V17 263) and Shane Kidd (V17 265) to implement.

### 2. Corpcapital's financial year ended 31 August 2002

- FH again audited the Cytech records in terms of SAAS.
- The Cytech audited accounts for the financial year ended September 2002 have been completed by the auditors. No material discrepancies with the management accounts were identified.

## J. HAMBURGER: STATEMENT

### APPENDIX 4: EXTERNAL VALUATION

1. In an investment banking Exco meeting of 12 May 2000 I was instructed to have an external valuation performed on Netainment.
2. Again on 14 July 2000 it was agreed in an Investment Banking Exco meeting that a major auditing firm would be requested to undertake a thorough valuation of the business. It was noted that I was in discussions regarding external valuations with Arthur Andersen, PwC and KPMG.
3. I approached PwC (London) to do the valuation of Netainment. I knew that PwC (London) had a highly specialized valuation department (I had interacted with them previously). PwC have strict client acceptance procedures. Given my historical working relationship I was able to give them the requisite comfort about the business to allow them to make a proposal to us.
  - 3.1 I spent time interfacing with the PwC valuation department to give them background information on the industry and the nature of the business. I supplied PwC with industry reports. In addition they did their own internal research.
  - 3.2 This culminated in their proposal to Netainment in June 2000 (refer V11 402). PwC proposed a fee based on time spent and estimated that it would cost approximately £80-100 000.
  - 3.3 The fee seemed exceptionally large. I tried to get competing quotes from other advisors. The process was very time consuming and the indications were that the cost would be no less than PwC.
4. The size of PwC (London) fee and the difficulty I was having in timeously securing an alternative was conveyed to Fisher Hoffman and the Corpcapital executive directors.
5. I understood that Peter Kay subsequently advised against an independent valuation. His rationale was that Corpcapital must value the asset consistently with accounting practice. His feeling was that the cost of the external valuation would outweigh any benefit from having the valuation done externally. Peter's audit process would provide the necessary independent attention to ensure that the assumptions underlying the valuation were reasonable.

J. HAMBURGER: STATEMENT

**APPENDIX 5: OWNERSHIP ISSUES**

1. No member of Corpcapital management or its executive has any personal interest in Cytech, whether directly or indirectly. Sean Rose and Tal Harpaz are beneficial and not nominee owners of their combined 47.5% interest in Cytech.
2. In all the important negotiations with both Sean and Tal they were independently represented and the discussions were heated. Their advisors included:
  - 2.1 Edward Nathan (M. Segerman); and
  - 2.2 Mishcon de Reya (Larry Nathan)
3. Further evidence of their ownership is evidenced from the following interactions and disclosures:
  - 3.1 One of the points raised during the negotiation of the Amalco merger agreements was that Corpcapital wanted to transfer its shareholding in Amalco to a venture capital fund it was in the process of forming without this triggering any rights of pre-emption. The lawyer to English Harbour (Sean Stevens of Fasken Martineau) mentioned that Sean and Tal's beneficially held shares must be bought pro-rata (V1559).
  - 3.2 Sean and Tal were executive directors of Aqua. Subsequently Sean resigned as a director and Tal became non-executive. At each financial year-end, Sean and Tal were required to make directors' declaration of their interests in contracts in terms of section 234 (3) (a) of the Companies Act. Their declarations are included in the file (refer V15 80,; V18 23 to 26 : V18 219 and 220). Sean and Tal initially made a declaration that they were indirect shareholders in Netainment "but change this to read "indirect non beneficial shareholder"
  - 3.3 In my brief to Janet Barnes of Deloitte and Touche Human Resources (V15 153 ) I disclose that Sean and Paul Sudolski own (implying beneficially) 12.5% (50% of 50% of 47.5%)and 10% of Amalco respectively. I advise that she should use this fact two when determining an appropriate remuneration packages for them.
  - 3.4 Refer Evan Hoff's schematic group structure on V17 251 where he notes that Rose/Harpaz are shareholders in Netainment. Review V18 61 email from

## J. HAMBURGER: STATEMENT

Schindler's to me. Mandy Feldman requires the ultimate beneficial owners of Netainment to sign an agreement. She refers to Sean and Tal signing on behalf of the trusts.

- 3.5 In a January 2001 meeting in London with Jeff, Sean, Tal and myself, all parties agreed to consider Netainment purchasing Aqua. Sean and Tal were concerned that the proposed transaction whereby Cytech purchased Aqua for shares in Cytech could result in them having less shares than us in an enlarged Cytech/Aqua group. They insist that Corpcapital proposed a mechanism whereby the ultimate shareholding in the enlarged group would remain equally split between Sean/Tal and Corpcapital. (V19<sub>2</sub> to<sub>3</sub>).
- 3.6 I disclosed to PwC London that Sean and Tal are the beneficial owners of 47.5% of the business (V19<sub>18</sub>) during the Project Rider initiatives.

## HAMBURGER: STATEMENT

### APPENDIX 6: CYTECH BONUS ISSUE

1. In September 2000 Sean and Tal, believing the Amalco merger to be near final and in light of the undisputed operational success of the casino requested a bonus payment of \$1m. Corpcapital debates the payment of this bonus at length.
2. I prepared a Memo to Martin, Benji and Jeff relating to the Netainment bonus payments requested by Sean and Tal (V15<sub>136</sub>). There was much debate around this bonus issue.
3. On 12th December 2000 I received an email from Sean confirming that Tal and him had paid themselves the bonus proposed in his September 18 email (V15<sub>300</sub>). Corpcapital viewed this unauthorised action in the most serious light.
4. Please refer various correspondences with respect to this issue on V15<sub>328,329,330,354</sub>.
5. Jeff was in Thailand at the time. Notwithstanding, he was immediately informed telephonically and through fax of Sean and Tal's actions.
6. Corpcapital relied on Sean and Tal to run Netainment day-to-day. (Corpcapital understood this risk and over time I became more operationally focused to reduce this reliance on the two individuals.) and therefore Corpcapital was reluctant to be "heavy handed" or aggressive in our response to their actions. Additionally we needed them to close the Amalco deal (We welcomed Paul Sudolski's role in Amalco to balance the Shaun/Tal entrepreneurial personality)
7. Corpcapital's response (principally by Benji but with input from Jeff, Martin and myself) was immediate, firm and clear about our position.
8. This incident was a microcosm of the dynamic in the relationships between Corpcapital and Shaun/Tal.
9. Jeff requested that I prepare a memorandum summarising the bonus issues. I respond in a memo dated 11 January 2001 (copied to Martin and Benji V16 a). This memo summarised the historic bonuses, financial results, balance sheet and referred to the Deloitte salary benchmark report that Benji had commissioned. I suggest that, given the difficulty I am having in arranging for the financial statements to be presented, we make part of their bonus conditional on completing a satisfactory audit.
10. On 19th February 2001 Jeff agreed with Tal that the executive bonuses for the periods ending December 2000 was \$700 000 payable \$600 000 immediately and \$100 000 on

## J. HAMBURGER: STATEMENT

the satisfactory conclusion of an audit of the Netainment business. The bonus was extraordinary in size and represented the superb growth of the business since inception. Corpcapital made the point to Sean and Tal that future bonuses would be calculated with, reference to year-on-year performance.

J. HAMBURGER: STATEMENT

**APPENDIX 7: MY INTERACTION WITH MR FRANGOS**

1. I detail below the chronology of my interaction with Mr Frangos.
2. I have never withheld any information from Mr Frangos. I never sought to delay the communication of information to him. At no time was I influenced to misrepresent or embellish information that I gave him.
3. During my meetings with Mr Frangos I was honest and forthcoming at all times.
4. The chronology of my dealings with Mr Frangos are as follows:
  - 4.1 In November 2001 I was requested to prepare a presentation on the Cytech valuation to the board of directors of Corpcapital (V18<sub>305</sub>). Although the presentation was ready, and I waited outside the boardroom, I was never called on to make the presentation.
  - 4.2 On 31 May 2002 I am asked to join a meeting with Mr Frangos and Martin on short notice. In this meeting I was questioned by Mr Frangos about various issues relating to the Cytech valuation. I dealt with most issues at the time and where I was not able to answer, I committed to get back to him.
  - 4.3 I subsequently discussed timing for the delivery of the further information with Mr Frangos. He was relaxed when I told him that I had concomitant work pressure. He informed me that it would be acceptable to deliver my response to him after he returned from the US Open.
  - 4.4 On 21 June 2002 I delivered a detailed document to Mr Frangos answering comprehensively his questions raised at the time of the 31 May 2002 meeting (V20<sub>205</sub>).
  - 4.5 I subsequently met Mr Frangos a few days after the delivery of the document to answer further questions and explain the document.
  - 4.6 Mr Frangos had further questions. Notwithstanding that the answers to his questions could be substantially found in the 21 June 2002 document, I responded further in a document faxed to Mr Frangos on 9 July 2002 (V20<sub>303</sub>). Mr Frangos never reverted back to me directly with any further questions.

J. HAMBURGER: STATEMENT

5. I subsequently understood from Jeff and Benji that Mr Frangos was not satisfied and I received a copy of Mr Frango's submission to Eric Ellerine, Tom Wixley and Wim Trengove of 14 October 2002 (V20eo).
6. I was requested by Benji on or about 20 October 2002 to prepare a detailed submission for the purpose of the Saxon meeting of 25 October 2002. My submission is included in the Cytech bundle (V20<sub>175</sub>, V20<sub>205</sub>, V20<sub>293</sub>, V20<sub>303</sub>).

**APPENDIX 8: MY BONUS**

1. I received a bonus of R1.5m and R1m in respect of the Corpcapital's financial years ended 31 August 2000 and 2001 respectively
2. During the relevant October's performance review process I was told that my performance in respect of the following matters was considered relevant for the purpose of determining the quantum of these bonuses:
  - 2.1 The operational and corporate success of the assets managed including:
    - Cytech: operating performance and English Harbour merger initiatives, IMS software corporate initiatives;
    - Aqua Online: successful reverse listing concluded;
  - 2.2 The following qualitative factors were also considered:
    - My role within Corpcapital had been expanded to include the management of Investment Banking division. I was responsible for the administration of the division, the attendance of monthly Investment Banking Exco's and the division's marketing initiatives.

## J. HAMBURGER: STATEMENT

### APPENDIX 9: ENGLISH HARBOUR MERGER

1. In early May 2000 Sean informed Corpcapital of a potential opportunity to merge the Netainment operations with a Canadian based on-line casino called English Harbour. Paul Sudolski, an ex-investment banker, was the CEO of this business.
2. Netainment and English Harbour operated its casinos on the Microgaming casino platform. Given the highly scalable nature of on-line casino operations, it was understood that the management of both casino operations could occur off a single back office infrastructure.
3. The two businesses had almost identical corporate and operational structures. A proposed merger could eliminate duplicate infrastructure immediately. The cost savings and other synergies were obvious and substantial.
4. Paul shared our enthusiasm for a London listing. He was impressed with the relationships we had developed with London institutions and the progress we had made to list there.
5. Paul had contemplated an English Harbour listing previously (refer Business Plan on V1 Isis) He believed that a London listing would be more favourable than his planned US listings.
6. Jeff was informed of the merger potential and was very excited.
7. I met Paul, Sean and Tal in London in May 2000 to discuss the merger opportunities.
8. I circulated a memorandum highlighting my May 2000 London trip (Vllaoe). The memo was circulated to Martin, Jeff and Benji, David Liebowitz and Kevin Joselowitz.
9. Inherent in the merger discussions was a conflict of interest between Aqua and Netainment. These issues were identified early in the negotiations and were dealt with by engaging with disinterested members of the Aqua board (Jonathan Schneider and Brent Shahim) early and often in the process.
10. English Harbour indirectly owned its back office administration business. Netainment's infrastructure was outsourced to Aqua. A merger of the Aqua and English Harbour infrastructures was necessary to fully exploit operational synergies. Sean and Tal strongly believed that the current monthly Aqua administration expense was not market related. The Aqua fee was calculated at 12.5% of revenue. The Netainment revenue had, however, grown in absolute terms to a level where the Aqua fee was not market related (no maximum fee was negotiated).

## J. HAMBURGER: STATEMENT

11. Aqua performed marketing and administrative functions for the Netainment casinos. Marketing was seen as a core competence of the casino Sean and Tal proposed that Netainment purchase the Aqua marketing team to facilitate the English Harbour merger. It was considered necessary for the merged group ("Amalco") to own its own marketing team. *(After the English Harbour merger failed in March 2001, Netainment entered into a new long-term agreement with Aqua. This was negotiated between Brent Shahim and Sean Rose. The monthly fee to Aqua was reduced from 12,5% to 7,5% and the Aqua marketing team (4 people) were purchased for a consideration of \$600,000 payable over 12 months).*
12. The basis of agreeing relative values for the purpose of the Amalco merger was not determined conclusively in the London meeting of May 2000. It was proposed to consider relative values based on relative contributions of actual revenue and profit levels for the prior three months. Netainment's revenue and profits were approximately 20% and 40% lower than the equivalent English Harbour numbers (although the Netainment's profits included a very high Aqua fee relative to English Harbour's infrastructure costs) - refer V11<sub>310</sub>.
13. We argued that Netainment, notwithstanding its smaller size, had a better quality of earnings than English Harbour. This was because a high percentage of Netainment's clients was resident outside the US. These players were less susceptible to any US regulatory threats. Additionally, higher margins were earned on non-US players (the return on advertising spend in the non-US markets was particularly high and given the lack of competition these players tended to be more loyal and played for longer).
14. Paul Sudolski's CV is contained on V11<sub>311</sub>. My impression of Paul was that he was a professional manager and that he would complement the very entrepreneurial management style of Sean and Tal.
15. The corporate strategy to form Amalco was intensely debated at Corpcapital (Benji memo of May 2000 refers V11<sub>312</sub>). This was not a deal we were going to enter into lightly given the value of our asset and our own initiatives to list Netainment separately in London.  
  
English Harbour prepared a memorandum in anticipation of its own listing initiatives (May 2000) (V11<sub>215</sub>). Historic and projected revenue and profit numbers are presented (and shown below). These numbers give a good indication of comparable industry growth rates and the expectations for forward growth of Cytech's competitors.

	Actual Dec 1998	Actual Dec 1999	1 yr fwd Dec. 2000	2 yr fwd Dec. 2001	3 yrs fwd Dec 2002
Drop/ revenue (\$'m)	3.1	11	41.4	84.5	104.6
Profit (\$'m)	0.4	2.5	11.7	24.4	30.4
Growth in drop	-	267%	276%	104%	24%
Growth in profit	-	525%	368%	109%	25%
Margin (as a % of drop)	12,9%	23%	28%	28%	29%

The intention was to list the merged group. It was anticipated that the listing would attract a higher price for the Cytech shareholders than projected by Insinger for the Cytech stand-alone listing.

16. The conclusion I drew from the table above was that our competitors were experiencing similar explosive growth. Our business was not unique (or an aberration) to the industry. On the contrary, given our non-US customer base I felt Netainment had a relatively better business than its peers.

17. Jeff and I planned to meet Sudolski in Toronto in late June and early July 2000 to negotiate the Amalco merger. In anticipation, I sent off a list of relevant information required by Sudolski (V1137s). I do this in order to get a detailed understanding of the English Harbour business.

One of the key issues in the Amalco merger discussions was the MGS relationship. Sean, Tal and Paul believed that the Microgaming commercial relationship was unsustainable given the profit of the business. In Netainment's better months it paid an approximate \$750,000 royalty to Microgaming and obviously the temptation to develop proprietary software and leave Microgaming was great. Sean, Tal and Paul felt that MGS would eventually reduce its royalty terms. MGS competitors (software developers) could enter \* the market and offer a similar or superior product at lower usage fees. *(Ultimately this occurred.*

- *Playtech, for example is an Israeli based developer of on-line casino systems. Its software is regarded as being of relatively equal quality to MGSs. Playtech's royalty is calculated at a maximum of 15% of revenues.*
- *MGS recently (February 2003) - lowered its usage fee payable by its clients on their non-US business. The rate was lowered to 20% in an attempt to encourage clients to move their businesses away from America}.*

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18. David Leibowitz was requested to analyse the Netainment and English Harbour MGS agreements with a view to thoroughly understanding the parties legal position (V11 4is) in advance of the Amaico merger.
19. English Harbour and Netainment's businesses were dependent on Microgaming giving consent. English Harbour and Netainment had shared experiences in dealing with MGS (and the Moshal family). Often MGS would threaten to "switch-off the operating system. This was an unacceptable and untenable relationship with which to grow a business.
20. Jeff, Tal, Sean and I met Sudolski in Toronto from 25<sup>th</sup> June to 31 July 2000 to negotiate and finalise the terms of the Amaico deal. The outcome was successful as we negotiated a 50% holding for Netainment in Amaico. On this basis I prepared an English Harbour / Netainment memorandum of understanding brief (V12 17 ). The key features of the deal were:
  - 20.1 English Harbour and Netainment shareholders would participate equally in Amaico.
  - 20.2 The parties would list Amaico on AIM as soon as practically possible.
  - 20.3 The Netainment shareholders would undertake to purchase the marketing team from Aqua and release Sean from his service contract.
  - 20.4 Aqua would provide administration services to the enlarged group on arm's length basis for an extended term. *(We anticipated that Aqua would be prepared to levy a lower percentage fee but be more than compensated by providing a service to a much larger business. Given that Aqua's infrastructure was highly scalable, the increased revenues to Aqua (calculated with reference to the Amaico revenues) would more than offset the reduced fee percentage).*
  - 20.4 Microgaming consent was required to finalise the deal.
  - 20.5 Reciprocal due diligences would be performed.
21. My memo to Kevin, Benji, Martin, Sean and Tal of July 2000 summarised in detail the commercial terms of the proposed Aqua / Amaico contract for the supply of back office services. I was confident that the proposed terms would result in Aqua increasing EPS. Additionally, Aqua would secure an extended contract (3.5 years) with Amaico . The Aqua discussions included the purchase by Aqua of English Harbour's administration business for shares in Aqua.
22. It was contemplated that Aqua levy a fee to Amaico calculated at 3% of the total Amaico customer deposits. Netainment's experience was that 50% of customer deposits would

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- translate to revenue, therefore a 3% fee calculated with reference to purchases is an approximate equivalent to 6% calculated with reference to revenue).
23. In July 2000 we received the first drafts of the heads of agreement from Sudolski's lawyers. There followed significant debate and correspondence between the parties, culminating in a non-binding heads of agreement signed on 3 August 2000.
  24. It is contemplated that Paul would become the CEO and Sean the COO. As a consequence Paul would relocate to London.
  25. English Harbour was convinced that the Microgaming relationship was unsustainable. One of their requirements was that Amaico be free to consider alternative software providers on commercial terms. We obviously understood at the time that English Harbour shareholders may have commissioned the development of an alternative casino software platform. English Harbour required that Amaico use this software when complete at a license fee of 15%. Netainment shareholders agreed to this on the basis that the new software was of acceptable standard. A 'side letter' was drafted and signed to give the English Harbour shareholders comfort that Netainment would support this initiative (V12<sub>197</sub>)
  26. After a 7 August 2000 meeting I confirmed that Amaico would secure 'blue chip' advisors in London. In this regard:
    - 26.1 Clifford Chance was retained to perform initial work on the merger documents to ensure compliance with English law. LJKlaters were approached to become the solicitors to Amaico (22 August 2000).
    - 26.2 PwC (London) was approached to audit the business.
    - 26.3 Amaico representatives briefed Field Fisher Waterhouse in November 2000 to assist in jurisdiction! issues (V15 130). The Field Fisher Waterhouse opinion is contained in V15 239.
    - 26.4 Jonathan Swartz a UK advocate was engaged to advise Amaico on structuring matters.
  27. Sean and Paul Sudolski dictated the terms for their London based Amaico employment. It was agreed that disinterested English Harbour and Cytech shareholders' represented by John Warren and Benji negotiate the employment contracts. (Refer V13276 and V1331). Benji received authority from Amaico to engage Deloitte and Touche Human Capital in London to advise on an appropriate salary structure.

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28. A draft copy of the Sean Boss and Paul Sudolski proposed service and restraint of trade agreement is contained in V15 258 for completeness.
29. Paul Sudolski came to South Africa on 31st August 2000 to visit Corpcapital and review the Aqua operations. He was also impressed with the quality and extent of the Aqua infrastructure.
30. The disinterested board of Aqua directors approved the Amalco / AIM term sheet. Additionally they approved, conditionally, Sean's release from his service contract obligations. (V15 3)
31. The English Harbour Netainment binding merger agreement was signed on the 26th October (subject to obtaining Microgaming consent) (V14). This merger agreement contained the final Aqua term sheet (V14 38)
32. The Netainment due diligence of the English Harbour business took place in Toronto in late October early November 2000. Sean, Tal, an IT person (from Aqua) and I performed the work. The work program and findings are detailed on V1589. We obtained a high degree of comfort from the English Harbour numbers given that they operated off the same Microgaming accounting package. Our conclusion was that EH was a good business, was highly profitable and was growing. We were doing well to get 50% of the merged business.
33. The comparison of English Harbour to Netainment results is detailed on V1592. Netainment (King Solomon ("KS")) results are consistently below English Harbour's (in June the EH cash drop was 20% higher than Netainment's). (V1599-102 contains further comparison of the English Harbour results). The English Harbour monthly growth in revenue was particularly impressive.
34. In November 2000 Paul Sudolski and a colleague completed their due diligence of the Netainment business. They conducted their review in London using financial information extracted from the Microgaming accounting package. Paul's primary concern after his investigation was that our historic numbers (relative to English Harbour) did not warrant Netainment shareholders receiving 50% of Amalco. Notwithstanding his desire to renegotiate the price he concluded the due diligence.
35. MGS were not willing to provide consent easily (review correspondence in V16 233, V16 317, V16 331.)
36. In a conference call arranged between English Harbour (Paul) and Netainment (Sean, Tal, Jeff, Jade - in London) on 8th March 2001, all parties agreed to postpone the merger given Microgaming's unwillingness to provide consent.

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37. I understood at the time that Sudolski wanted to ensure that his alternative software arrangements were ready prior to any merger Paul subsequently left MGS and moved onto his new platform in 2001.
38. Paul has since initiated further merger discussions with Cytech in 2003.
39. In July 2002, as a result of a request by Martin, I met Tom Wixley to take him through the Cytech valuations. Tom was satisfied with the presentation.
40. In or around August 2002 I understood from Martin that PWC (Johannesburg) would be engaged to perform an independent valuation of Cytech.
41. I cooperated fully with PWC during their investigation.