IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF COLUMBIA

UNITED STATES OF AMERICA, Plaintiff, v. MICROSOFT CORPORATION, Defendant.	**MEMORANDUM OF THE UNITED STATES IN SUPPORT OF MOTION FOR PRELIMINARY INJUNCTION**

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UNITED STATES OF AMERICA,

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MEMORANDUM OF THE UNITED STATES IN SUPPORT OF MOTION FOR PRELIMINARY INJUNCTION

1. INTRODUCTION

"Microsoft dominates the world market for operating systems software that runs on IBM-compatible personal computers." *United States v. Microsoft Corp.,* 56 F.3d 1448, 1451 (D.C. Cir. 1995). On December 11, 1997, the U.S. District Court entered a preliminary injunction prohibiting Microsoft Corporation ("Microsoft") from requiring computer manufacturers to license and preinstall Microsoft's Internet browser software as a condition of licensing Microsoft's Windows 95 computer operating system software. The Court found, among other things:

> [T]he marketplace, and the public generally, will benefit from the issuance of a preliminary injunction. . . . Microsoft's licensing strategy is allegedly designed to overwhelm the developing competition in the browser market (which at the moment Microsoft does <u>not</u> dominate) before it becomes established, thereby perpetuating Microsoft's operating system monopoly. . . . [T]he probability that Microsoft will not only continue to reinforce its operating system monopoly by its licensing practices, but might also acquire yet another monopoly in the Internet browser market, is simply too great to tolerate indefinitely until the issue is finally resolved." 980 F. Supp. 537, 544 (D.D.C. 1997).

The United States has filed today and served a complaint under Sections 1 and 2 of the Sherman Act, 15 U.S.C. §§ 1 and 2, seeking to enjoin Microsoft's continuing efforts (1) to maintain its operating system monopoly by exclusionary and predatory conduct, (2) to unreasonably restrain competition through various exclusionary and predatory practices, including tying and other exclusionary agreements, and (3) to attempt to monopolize the Internet browser market. The United States brings this motion for a preliminary injunction to preserve the competitive *status quo* during the pendency of this litigation -- in particular, to enjoin Microsoft from continuing to foreclose competition among Internet browsers by, among other things, tying its Internet browser ("Internet Explorer" or "IE") to Microsoft's Windows 98 operating system.

Over the past two years, Microsoft has engaged in a pattern of illegal and exclusionary conduct designed to deny personal computer makers, Internet Service Providers, Internet Content Providers, independent software vendors, and consumers the freedom to choose the Internet products that are installed on their computers. Unless enjoined, Microsoft will carry out the next significant step in this continuing pattern of anticompetitive conduct. Microsoft's impending illegal actions, coupled with its ongoing exclusionary conduct, will maintain the software giant's existing monopoly power over personal computer operating systems and extend that monopoly to another critical market -- the market for Internet browsers.

On or about June 25, 1998, Microsoft intends to release Windows 98, the successor to its Windows 95 personal computer ("PC") operating system, to the market. Today, Microsoft will provide the final code for Windows 98 to PC original equipment manufacturers ("OEMs") for preinstallation on PCs the OEMs sell. When it does so, Microsoft will once again use its monopoly power to require OEMs to license and distribute its Internet browser, even if those OEMs wish to distribute only a competing browser, or no browser at all, with their PCs.

Microsoft's monopoly power in the market for personal computer operating systems is not subject to genuine dispute. As PC OEMs know, they have no commercially reasonable alternative to Microsoft's operating systems. The imminent release of Windows 98, in which Microsoft has intentionally hardened the illegal tie-in of its Internet browser to its operating system, creates an urgent need for a preliminary injunction:

- Packard Bell executive Mal Ransom testified that there were no "commercially

feasible alternative operating systems" to Windows 98. *M. Ransom 3/98 Deposition Transcript Excerpts ("Ransom Dep."), p. 19, line 23 - p. 20, line 1.*[1]

- Micron executive Eric Browning asserts: "I am not aware of any other non-Microsoft operating system product to which Micron could or would turn as a substitute for Windows 95 at this time." *Declaration of E. Browning ("Browning Decl."), ¶ 11.*
- Hewlett Packard executive John Romano testified that HP had "absolutely no choice" except to install Windows on its PCs. *J. Romano Deposition Transcript Excerpts ("Romano Dep."), p. 49, line 15, p. 50, line 12.*
- Gateway executive James Von Holle testified that Gateway had to install Windows because "We don't have a choice." *J. Von Holle 9/97 Deposition Transcript Excerpts ("Von Holle 9/97 Dep."), p. 37, line 5 - p. 41, line 13*; *Exhibit 1 (GW 26521-27).* Mr. Von Holle has testified that if there were competition to Windows, he believed such competition "would drive prices lower" and promote innovations *Von Holle 9/97 Dep., p. 38, line 20 - p. 39, line 6.*

Microsoft's operating system monopoly is protected by high barriers to entry, including the large number of software applications that will run on Windows but not on other operating systems. PC users generally want the most, and the most up-to-date, software applications available. Application programs must be able to connect to (be "compatible" with) an operating system in order to run. The operating system is in effect a necessary software layer (or "platform") between the PC hardware and the applications programs.

Because it would be prohibitively difficult, time-consuming, and expensive to create an alternative operating system that would run the many applications that run on Windows, a potential new entrant faces a high barrier to successful entry. This applications programming barrier to entry tends to be self-perpetuating. Windows is the dominant operating system; as a consequence, more applications are written to run on it; and because more applications are

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[1]All deposition and declaration testimony cited in this Memorandum is hereafter referred to by the name of the deponent or declarant. The pertinent testimony is set forth in alphabetical order in the attached Appendix of Declarations and Deposition Excerpts.

written for Windows, Windows dominance is further entrenched -- which in turn leads to more application programs being written for it than for other operating systems, and so on.

As Microsoft recognized in 1995, a potential threat to the continuation of the software applications barrier, and hence to the continuation of Microsoft's operating system monopoly itself, arose from the growing popularity of the Internet and the World Wide Web ("the web"). Internet browsers -- specialized software programs that allow PC users to locate, access, and display content and applications located on the web -- are essential for quick, easy, and efficient use of the web and have been instrumental in building the Internet's popularity. No other product duplicates or fully substitutes for their functionality.

Because browsers can help to overcome the incompatibility between different operating systems by allowing applications to run on a variety of other operating systems, browsers can reduce or eliminate the key barrier to entry which protects Microsoft's operating system monopoly. Microsoft's CEO Bill Gates referred in May 1995 to this possibility as the threat that Netscape's Navigator would "commoditize" the operating system. *Exhibit 2 (MS6 5004549-58), B. Gates 5/26/95 e-mail.*

Internet browsers pose a competitive threat to Microsoft's operating system monopoly in two basic ways. First, Netscape's browser is the most important means by which a new programming language known as "Java" is made available to computer users. Java is designed in part to permit applications written in it to be run on different operating systems (or "across platforms"). The more Java is distributed and used to write application programs, the more a critical barrier to entry protecting Microsoft's monopoly power is reduced. Microsoft has recognized that competing browsers can increase the proliferation and use of Java, and in so doing can threaten Microsoft's operating system monopoly.

Second, Microsoft has also recognized that Netscape's "Navigator" browser is itself a platform to which many applications were being written, and to which (if it thrives) more and more applications would be written. Since Netscape's browser can be run on virtually any PC operating system, applications written to Netscape's browser can also be used with different operating systems. Accordingly, the success of Netscape's browser created an alternative platform that, standing alone, threatened to reduce or eliminate a key barrier protecting

Microsoft's operating system monopoly.

To respond to the competitive danger posed by Netscape and Java (and more broadly the promise of Internet computing as a substitute for the Windows monopoly), Microsoft embarked on an extensive campaign to market and distribute its own Internet browser, which it named "Internet Explorer" or "IE." Microsoft executives have described this campaign as a "jihad" to win the "browser war." A January 5, 1997, presentation to Microsoft CEO Bill Gates on how to respond to the Java threat emphasized "Increase IE share" as a key strategy. *Exhibit 3 (MS7 005529-44).*

With its resources and programming technology, Microsoft was well positioned to develop and market a browser in competition with Netscape. Indeed, ongoing competition on the merits between Netscape Navigator and Microsoft Internet Explorer could have been expected to result in greater innovation and the development of better products at lower prices. The competitors had offsetting advantages -- Microsoft with its size and dominant position in desktop software, and Netscape with its position as the browser innovator and leading browser supplier -- and the benefit to consumers of product differentiation could have been expected to sustain continued competition on the merits between these companies into the future.

Microsoft, however, has been unwilling to compete purely on the merits. Instead, Microsoft began, and continues today, a pattern of anticompetitive practices designed (1) to stifle the potential competitive threat to its operating system monopoly, and (2) to extend its monopoly to the Internet browser market.

In May 1995 Microsoft tried to convince Netscape to enter into an agreement not to compete and to divide the browser market. Microsoft proposed in part that Netscape provide the sole browser for non-Windows 95 operating systems and that Microsoft provide the sole browser for Windows 95 operating systems. When Netscape refused, Microsoft reacted -- it began a pattern of exclusive dealing arrangements, agreements to not distribute or promote competitive browsers, tie-ins, and other exclusionary and predatory conduct that excludes competition on the merits, robs OEMs and consumers of the opportunity to make their own choices, and deters innovation.

Browsers often are installed as part of the software provided when purchasing a new

computer from an OEM. PC users also frequently obtain browsers through their Internet Service Provider (or "ISP"). Microsoft recognizes that "the ISP channel and the OEM channel are the most important channels for distribution." *C. Myhrvold Deposition Transcript Excerpts ("Myhrvold Dep."), p. 43, lines 7-18.* Since May 1995, Microsoft has substantially foreclosed non-Microsoft browsers from the ISP channel by entering into agreements with Online Service Providers (including America Online and CompuServe) and other leading ISPs that require those providers to distribute and promote Internet Explorer and *not* to distribute and promote competitive browsers. These agreements require ISPs to:

- distribute and promote Internet Explorer to their subscribers exclusively or nearly exclusively;
- refrain from expressing or implying to their subscribers that a competing browser is available; and,
- limit the percentage of competing browsers they distribute, even in response to specific requests from customers.

Microsoft entered into similarly restrictive agreements with Internet Content Providers ("ICPs").

Even though it had cost Microsoft hundreds of millions of dollars to develop, test and promote Internet Explorer, Microsoft began to distribute Internet Explorer without charge even though Netscape, the leading browser supplier at that time, was charging OEMs for its browser. As Paul Maritz, Microsoft Group Vice President in charge of the Platforms Group, was quoted in the *New York Times* telling industry executives: "We are going to cut off their air supply. Everything they're selling, we're going to give away for free." *Exhibit 4, New York Times 1/12/98*. As reported in the *Financial Times*, Microsoft CEO Bill Gates likewise warned Netscape (and other potential Microsoft challengers) in June 1996: "Our business model works even if all Internet software is free. . . . We are still selling operating systems. What does Netscape's business model look like (if that happens)? Not very good." *Exhibit 5, Financial Times 6/10/96.*

In fact, Mr. Gates did not stop at free distribution. Microsoft set out to do whatever it took to make sure that significant market participants did not distribute Netscape's browser. For example, Microsoft tried to convince Intuit, among the most significant application software

developers in the United States, not to distribute Netscape's browser. Mr. Gates was blunt, as he reported in a July 1996 internal e-mail:

> I was quite frank with him [Scott Cook, CEO of Intuit] that if he had a favor we could do for him that would cost us something like $1M to do that in return for switching browsers in the next few months I would be open to doing that. *Exhibit 6 (MS6 6007642-43), B. Gates 7/24/96 e-mail.*

Moreover, Microsoft tied its Internet Explorer browser to Windows 95, requiring OEMs to preinstall IE (and to agree not to remove all or part of it) as a condition of obtaining a license to Windows 95. Microsoft continued that tie until January 1998, when it came into compliance with the Court's Order of December 11, 1997, prohibiting such tying and barring Microsoft's use of its Windows monopoly to induce OEMs to select and distribute IE.

Microsoft's anticompetitive conduct has been achieving its goal. Microsoft's share of the browser market increased dramatically from 3% or 4% in early 1996 to approximately 50% in early 1998.

Microsoft's latest anticompetitive act is to tie its IE browser to Windows 98, the next version of its Windows operating system, which is being released to OEMs today and will be available to consumers on June 25, 1998. Microsoft will require OEMs as a condition of obtaining Windows 98 to agree not to remove IE or replace it with a competing browser. Microsoft's Windows 98 tie-in threatens to foreclose competing browsers from the OEM channel, the second of the two "most important channels of distribution" for browsers.

It will be a commercial necessity for OEMs to install Windows 98, so virtually every new PC shipped to end users will come with Microsoft's browser. Microsoft's tie of its Internet browser to Windows 98 is illegal under both Sherman Act Section 1 (as a restraint of trade) and Section 2 (as unlawful maintenance of Microsoft's operating system monopoly and as attempted monopolization of the Internet browser market).

Internet browser software is a separate product from operating systems. For example:

- IE 4.0, like previous versions of IE, was (and will be) distributed by Microsoft as a separate product though ISPs, retail outlets, and other channels, and future versions of IE will be developed;
- Microsoft and the industry track browser market share separately;

- Internet browsers perform different functions from those of operating systems;
- Microsoft promotes, and enlists others to promote, the distribution and use of IE as a separate product;[2]
- Microsoft has consistently treated and referred to its browser software as a separate product,[3] and not as a component of the operating system, both internally and in agreements with other companies;[4]
- ISPs consider IE to be a product separate from Windows and Microsoft markets it to them as such. *C. Myhrvold Dep., p. 26, line 21 - p. 27 line* 9; and
- Microsoft develops and markets IE for non-Microsoft operating systems.

There is also demand for Internet browsers separate from the demand for operating systems. For example:

- Many PC users do not need or want a browser;
- For many PC users, the forced inclusion of a browser with the operating system is a significant negative -- including corporate customers who do not want their employees connected to the Internet[5] and customers who do not want to devote

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[2]*See, e.g. Exhibit 7 (MSV 10002, MSV 10010, MSV 10014, MSV 10025, MSV 10031); Exhibit 8 (MS6 6008291); Exhibit 9 (MSV 0005734); Exhibit 10 (MSV 0005703).*

[3]Over "the last couple of years" Microsoft was told by its counsel to be "careful" not to refer to its browser software in such a way that it appeared that the software was a separate product. *P. Maritz Deposition Transcript Excerpts, p. 106, lines 5-12; Exhibit 16 (MS7 005306).* More recently, Microsoft executives became "very concerned" that statements in the ordinary course of business made IE "appear separate" and concluded it was "critical" that there be "a thorough walk-through looking for places in the UI [user interface] that can be corrected" and that there be "a sweep" of the IE website to remove references inconsistent with Microsoft's present legal position. *Ibid*. It was agreed that there would be "a review of win 98 by Microsoft executives" and "someone from legal staff" to "ensure IE is properly presented." *Ibid*.

[4]*Exhibit 11 (MS6 6010279-85); Exhibit 12 (MS7 0005728-38); Exhibit 13 (MS6 6008815-20); Exhibit 7 (MSV 10008); Exhibit 14 (MS6 6010346); Exhibit 15 (MS7 004127); B. Silverberg Deposition Transcript Excerpts ("Silverberg Dep."), p. 19, lines 6-22; J. Kempin 10/97 Deposition Transcript Excerpts ("Kempin 10/97 Dep."), p. 76, lines 13-25.*

[5]*Y. Mehdi Deposition Transcript Excerpts ("Mehdi Dep."), p. 34, lines 6-16; D. Cole Deposition Transcript Excerpts ("Cole Dep."), p. 50, line 2 - p. 51 line 25; M. Ransom 3/19/98 Dep. p. 9, line 14 - p. 10, line 4; B. Chase Deposition Transcript Excerpts ("Chase Dep."), p. 80, line*s 10-17.

disk space to unneeded functions; and

- A majority of all browsers distributed to date have been distributed to users who already had a PC with an operating system installed.

There is no reason grounded in efficiency or market demand for Microsoft to enforce its contractual restrictions that prohibit OEMs from offering consumers an unbundled version of Windows and Internet Explorer. In fact:

- Microsoft executive Chris Jones noted in 1995 that some OEMs "want to remove the [IE] icon from the desktop" but that the OEMs should be told "this is not allowed." *Exhibit 17 (MSV 0009129A);*
- In the Spring of 1996, Micron asked if it could delete IE from Windows. Microsoft refused;
- In June 1996, Compaq wanted to (and, for a time, did) remove the IE icon from the Windows desktop. Microsoft compelled Compaq to restore the icon by threatening to terminate Compaq's license to install the Windows operating system if Compaq did not comply; and
- "On several occasions, Gateway representatives have asked Microsoft to remove the icon for IE from the desktop, but Microsoft representatives have refused each request, saying the browser cannot be removed or sold separately. . ." *Exhibit 18 (Gateway 2000 Inc. 9/19/97 Answers to Interrogatories, p. 8).*

As the Court has previously found:

> Microsoft admits that it conditions its Windows 95 license agreements on OEMs agreeing to license and distribute IE, and the government has shown that there exists sufficient independent consumer demand for operating systems and Internet access software "so that it is efficient for a firm to provide" those products "separately," as Microsoft has concededly done. *U.S. v. Microsoft*, 980 F. Supp. at 544 (citing *Eastman Kodak Co. v. Image Tech. Serv., Inc.*, 504 U.S. 451, 462 (1992)).

Indeed, if the bundling of Windows and Internet Explorer were efficient, the combined product should thrive in a competitive market. But Microsoft has chosen to avoid the test of competition. Microsoft has deprived its customers of the competitive option of obtaining

Windows 98 without IE or without a browser at all; if a user wants Windows 98, he or she must take IE. The result is to foreclose customers' access to competing browsers.

- As recently as the Spring of 1997, Microsoft considered not bundling IE with Windows 98 (then code named "Memphis"). However, as described by Microsoft Senior Vice President James Allchin, it was decided "to tie IE and Windows together" in order to use the market power of the Windows operating system to foreclose competition among Internet browsers. *Exhibit 19 (MS7 05526)*.
- Microsoft's executive Kumar Mehta, after analyzing "how people get and use IE", concluded that "based on all the IE research we have done . . . it is a mistake to release Memphis [Windows 98] without bundling IE with it." *Exhibit 20 (MS7 004273)*.
- Microsoft concluded that if Windows 98 and IE "are decoupled, then Navigator has a good chance of winning," *Exhibit 21 (MS7 003001*) and that "if we take away IE from the O/S [operating system], most nav [Navigator] users will never switch to us." *Exhibit 20* (*MS7 004273*).
- As Microsoft executive Brad Chase wrote, "memphis is a key weapon in the IE share battle." *Exhibit 22 (MS7 004365)*.
- Microsoft's Christian Wildfeuer wrote on February 24, 1997: "It seems clear that it will be very hard to increase browser market share on the merits of IE 4 alone. *It will be more important to leverage the OS asset to make people use IE instead of navigator." Exhibit 23 (MS7 004343)* (emphasis added).
- On January 2, 1997, Allchin wrote that Microsoft needed to begin "leveraging Windows from a marketing perspective" if it was to defeat Netscape. "We do not use our strength -- which is that we have an installed base of Windows and we have a strong OEM shipment channel for Windows." Allchin emphasized: "I am convinced we have to use Windows -- this is the one thing they don't have. . . . We have to be competitive with features, but we need something more -- Windows integration." *Exhibit 19 (MS7 005526)*.

In the absence of preliminary relief, consumers will be deprived of their choice of

browsers, and consumers and the public will be deprived of the benefits of competition during the pendency of this action. Relief at the conclusion of this case cannot remedy the damage done to consumers and the public during the interim. In the absence of preliminary relief, there would be severe harm to competition. Microsoft's rivals would be foreclosed from the most effective means of distributing their browser to customers who, during the pendency of this case, purchase new PCs with Windows 98. Moreover, in part because of "network effects" and increasing returns to scale, Microsoft's continued market share gains will so strengthen its position (and so weaken its rivals' position) that waiting until the end of this case would likely require much more far-reaching relief. Thus, Microsoft's conduct threatens in economic terms irreversibly to "tip" the market in its favor. As the Court previously held with respect to Windows 95, "the cost of a compulsory unbundling of Windows 95 and IE in the future could be prohibitive." 980 F. Supp. at 544.

There will be no harm to Microsoft from the Court's granting the United States' requested preliminary relief. The Complaint and motion for preliminary injunction do not seek to prevent Microsoft from releasing and shipping Windows 98 on schedule. Nor do they seek to prohibit Microsoft from offering Windows 98 as Microsoft wishes to offer it -- combined with a browser -- to customers who *voluntarily* choose that combination. What the United States seeks is an Order during the pendency of this litigation enjoining Microsoft:

(1) from enforcing restrictive agreements which prevent OEMs, ISPs, and ICPs from choosing which browser or browsers they will distribute or promote, including any restrictions on the right of OEMs to remove Microsoft's browser or to implement the OEM's own screens or boot-up sequence;

(2) from distributing bundled versions of its operating system and its browser at a single price unless Microsoft provides a practical way of removing Internet browser functions and provides OEMs who do not wish to license the Microsoft browser an appropriate deduction from the royalty fee; and

(3) from distributing a bundled version of its operating system and its Internet browser unless Microsoft treats Netscape's browser the same as it own with respect to inclusion in and removal from the operating system.

This preliminary relief is essential to preserving competition, and protecting consumers and the public, during the pendency of the litigation.

The first form of preliminary relief (¶¶ 2a-d of the Complaint's Prayer for Relief) and the second form of preliminary relief (¶ 2f of the Prayer) are essential to suspend Microsoft's illegal conduct, and thus to prevent further competitive injury during the pendency of this action.

The third form of preliminary relief (¶ 2e of the Prayer) is necessary to preserve the competitive *status quo*, and to prevent Microsoft from securing irreversible dominance of the browser market. The best preliminary relief would be to require Microsoft to directly unbundle its operating system and browser products. Microsoft, however, has taken the position that Windows 98 has been designed to make that difficult and time consuming. In order to avoid simply enjoining the distribution of a bundled version of Windows 98 at this time (and thereby perhaps substantially delay its distribution), the United States seeks the more limited remedy of requiring Microsoft to include Netscape's browser on the same basis of Internet Explorer.

The equal treatment of Netscape's browser (either by unbundling Internet Explorer from Windows 98 or by bundling both Internet Explorer and Netscape's browser) is necessary to prevent Microsoft from conferring on its Internet Explorer browser a continued competitive advantage over its only significant browser rival, and thereby tip the browser market to Internet Explorer, during the pendency of this litigation.[6]

Microsoft's public relations campaign notwithstanding, the company's plan to tie its Internet browser to Windows 98 and its exclusionary agreements with OEMs, ISPs, and ICPs are simply the raw use of Microsoft's monopoly power to foreclose consumer choice, to eliminate competition on the merits, to preserve and enhance its operating system monopoly by stifling a potential competitive threat, and to extend its monopoly to a vitally important new market. The Court should issue a preliminary injunction to prevent those competitive harms from arising while this litigation proceeds.

The United States requests an expedited briefing schedule and an immediate hearing on its motion for a preliminary injunction to prevent irreparable harm pending resolution of this matter.

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[6]Distribution of numerous, less well-established browsers both would not offer the prospect of preventing tipping of the browser market and would impose additional burdens on OEMs.

2. JURISDICTION

This Court has subject-matter jurisdiction pursuant to 28 U.S.C. §§ 1331, 1337. Section 4 of the Sherman Act, 15 U.S.C. § 4, confers jurisdiction on this Court to prevent and restrain violations of Sections 1 and 2 of the Sherman Act, 15 U.S.C. §§ 1, 2.

3. THE LEGAL STANDARD FOR ISSUING A PRELIMINARY INJUNCTION

In an action brought by the United States to enforce the antitrust laws, a preliminary injunction is appropriate if the United States shows a likelihood of success on the merits and if the balance of equities tips in its favor. *United States v. Siemens Corp.*, 621 F.2d 499, 506 (2d Cir. 1980). This Circuit traditionally considers and balances four factors when determining whether a preliminary injunction should be issued: (1) whether the plaintiff has a substantial likelihood of success on the merits; (2) whether the plaintiff will suffer irreparable harm if the injunction is denied; (3) whether the defendant will suffer a disproportionate injury if injunctive relief is granted; and (4) whether the public interest favors the issuance of the preliminary injunction. *Taylor v. Resolution Trust Corp.*, 56 F.3d 1497, 1506 (D.C. Cir. 1995); *Washington Metro. Area Transit Comm'n v. Holiday Tours, Inc.*, 559 F.2d 841, 843 (D.C. Cir. 1977). This Circuit has noted, though, that the four-part test is a "flexible one" and that "[i]njunctive relief may be granted with either a high likelihood of success and some injury, or vice versa." *Population Institute v. McPherson*, 797 F.2d 1062, 1078 (D.C. Cir. 1986). As demonstrated below, all four factors strongly support granting a preliminary injunction here.

4. THE UNITED STATES HAS A SUBSTANTIAL LIKELIHOOD OF SUCCESS ON THE MERITS

Underlying all of the United States' allegations in this case are Microsoft's anticompetitive and exclusionary efforts to hinder opportunities of competing Internet browsers as a way to maintain and extend its operating system monopoly. Microsoft's anticompetitive agreements violate Section 1 of the Sherman Act; and its conduct, viewed both individually and in the

aggregate, also violates Section 2 of the Sherman Act.

a. Microsoft Has Acted Unlawfully To Maintain Its Operating System Monopoly In Violation Of Sections 1 and 2 Of The Sherman Act

To establish monopolization in violation of Section 2, the United States must show two elements: (1) the possession of monopoly power in the relevant market, and (2) the willful acquisition or maintenance of that power, as distinguished from growth or development as a consequence of a superior product, business acumen, or historic accident. *United States v. Grinnell Corp*., 384 U.S. 563, 570-71 (1966); *see also Southern Pacific Comm. Co. v. AT&T*, 740 F.2d 980, 1000 (D.C. Cir. 1984).

The first element of a monopolization claim -- monopoly power -- is "the power to control market prices or exclude competition." *United States v. E.I. duPont de Nemours & Co.*, 351 U.S. 377, 391 (1956). "[T]he material consideration in determining whether a monopoly exists is not that prices are raised and that competition actually is excluded, but that power exists to raise prices or to exclude competition when it is desired to do so." *American Tobacco Co. v. United States*, 328 U.S. 781, 811 (1946).

The second element of a monopolization action is "the willful acquisition or maintenance of [monopoly] power as distinguished from growth or development as a consequence of a superior product, business acumen, or historic accident." *Grinnell*, 384 U.S. at 570-71. This requires the Court to determine whether the monopolist "impaired competition in an unnecessarily restrictive way." *Aspen Skiing Co. v. Aspen Highlands Skiing Corp.*, 472 U.S. 585, 605 (1985). "If a firm has been attempting to exclude rivals on some basis other than efficiency, it is fair to characterize its behavior as predatory." *Ibid*. (internal quotations omitted). Furthermore, "[w]here a defendant maintains substantial market power, his activities are examined through a special lens: Behavior that might otherwise not be of concern to the antitrust laws -- or that might even be viewed as procompetitive -- can take on exclusionary connotations when practiced by a monopolist." *Eastman Kodak Co. v. Image Tech. Servs, Inc.*, 504 U.S. 451, 488 (1992) (Scalia, J., dissenting) (citing 3 P. Areeda & D. Turner, *Antitrust Law* ¶ 813, at 300-02 (1978)).

A monopolist also violates Section 2 when it enters into anticompetitive agreements that

serve to maintain its market power. Such agreements also violate Section 1 of the Sherman Act, and it is settled that a monopolist violates Section 2 if the monopolist has "maintained his strategic position, or sought to expand his monopoly, or expanded it by means of those restraints of trade which are cognizable under [Sherman Act] § 1." *United States v. Griffith*, 334 U.S. 100, 106 (1948); *United States v. United Shoe Mach. Corp.*, 110 F. Supp. 295, 342 (D. Mass. 1953), *aff'd per curiam*, 348 U.S. 521 (1954); *Barry Wright Corp. v. ITT Grinnell Corp.*, 724 F.2d 227, 239 (1st Cir. 1983).

Here, Microsoft's agreements with ICPs, ISPs (including Online Service Providers ("OLSs")), and OEMs, unlawfully maintain Microsoft's monopoly power in violation of Section 2 on both grounds: They draw on Microsoft's monopoly power to exclude competition on a basis other than efficiency, thereby tightening Microsoft's grasp on the operating system market; and they violate Section 1's proscription on employing anticompetitive agreements to maintain monopoly power.

i. *Microsoft Possesses Monopoly Power In The Operating System Market*

Microsoft has monopoly power in a well recognized market -- operating systems for Intel-compatible personal computers. Microsoft's "Windows" monopoly is shown by its high market share, with Windows 95 installed on almost all consumer PCs sold over the last three years and with Windows 98 to be preinstalled on virtually all personal computers sold beginning in June 1998. The barriers to entry in this market are very high.

(1) There Is A Relevant Market For Desktop PC Operating Systems

A relevant product market consists of "products that have reasonable interchangeability for the purpose for which they are produced." *United States v. E.I. duPont de Nemours & Co.*, 351 U.S. 377, 404 (1956); *see also SmithKline Corp. v. Eli Lilly & Co.*, 575 F.2d 1056, 1063 (3d Cir.) (the relevant product market consists of "those groups of producers which, because of the similarity of their products, have the ability, actual or potential, to take significant amounts of business away from each other"), *cert. denied*, 439 U.S. 838 (1978).

The relevant product market in this case is the market for "desktop" (as distinguished from "server" operating systems, ordinarily used to control the operation of servers coordinating the operation of networks of personal computers) PC operating systems that are run on Intel

x86/Pentium (or Intel-compatible) microprocessors. Competition from non-Intel compatible operating systems does not effectively constrain the pricing of Intel compatible operating systems. *Declaration of David Sibley ("Sibley Decl."), ¶ 8*. Most, if not all, PC OEMs see no alternative to preinstalling Intel-compatible operating systems on the PCs they build and sell.[7] The relevant geographic market is worldwide.

(2) Microsoft Has Monopoly Power In The Relevant Market

Microsoft develops and licenses a variety of software products, including operating system products. The current Microsoft desktop operating system product is Windows 95. Windows 98, the newest update to the Windows desktop family, is on the verge of release.

(a) Microsoft Has An Extremely High Share Of The Operating System Market

High market shares are sufficient to support an inference of monopoly power unless the market is characterized by factors such as ease of entry that would negate the inference. *Grinnell,* 384 U.S. at 571; *United States v. Aluminum Co. of Am.,* 148 F.2d 416, 424 (2d Cir. 1945); *American Tobacco Co. v. United States,* 328 U.S. 781, 785 (1946). Here, Microsoft has long possessed a dominant share of the personal computer operating system market.

Microsoft's market share has remained stable at approximately 90% for the last seven years, despite the efforts of experienced and well capitalized entrants such as IBM. *Sibley Decl., ¶ 14 & Table 1*. Indeed, even if the product market were defined to include operating systems for all PCs, not just those that are Intel-compatible, Microsoft's market share would be only slightly less, and it would still possess monopoly power. *Sibley Decl.¶¶ 8,14 n. 20*. In mid-1996, Microsoft estimated that 80% of the 23 million PCs projected to be sold in the United States from mid-1996 to mid-1997 would have Microsoft operating system products preinstalled on them by PC OEMs, while only 6% would have competing operating system products preinstalled. Microsoft projected that its OEM-installed operating system market share would be almost 86%

[7] *R. Brownrigg Deposition Transcript Excerpts ("Brownrigg Dep."), p. 9, line 2 - p. 10, line 23; Ransom 3/98 Dep., p. 12, line 20 - p. 13, line 13; Romano Dep., p. 49, line 15 - p. 52, line 4.*

by the end of mid-1997, while its competitors' shares would be only 2%.[8] These high market shares are themselves sufficient to raise a presumption of market power. *Aluminum Co. Of Am.*, 148 F.2d at 424.

(b) The Operating System Market Is Characterized By High Barriers To Entry And By "Network Effects" That Further Strengthen Those Barriers

Extremely high barriers to entry in the PC operating system market secure and reinforce Microsoft's monopoly power in that market. These barriers include: the considerable time and expense required to develop, test and market a new PC operating system; the lack of a sufficient installed base of users of the new operating system; and the difficulty in convincing OEMs to offer and promote a non-Microsoft operating system. These barriers are magnified and reinforced by "network effects" and "increasing returns in consumption" which result from the fact that the value to users of a particular good or service increases with the use of that good or service by others. *Sibley Decl. ¶¶ 11-13*.

Network effects are substantial in the operating system market. The more users a particular operating system has, the more applications software developers will write for that operating system; and that, in turn, will make the operating system more attractive to more users, resulting in positive feedback reinforcing its dominance. *Declaration of Franklin Fisher* ("*Fisher Decl.*"), ¶ III.A.3 These network effects give Microsoft a tremendous advantage. Applications written for one operating system will not work on another. Thus, the vast majority of users demand Windows because there are many times more applications written for Windows than for any other operating system. *Exhibit 28 (MS6 5003780-3786), Bob Muglia e-mail re: '97 Tools Vision (*"The Windows franchise is fueled by application development which is focused on our core APIs"*);*[9] *Exhibit 29 (MS6 5005721), Winning the Internet Platform Battle, Brad Chase,*

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[8]*See Exhibit 24 (MS6 6006356, excerpt from MS6 6006353-6006540) Microsoft North America FY 97 Reviews; see also Exhibit 25 (MS6 6000022) Microsoft OEM Sales FY '96 Midyear Review, Joachim Kempin, 1/22/96; Exhibit 26 (MS6 6001734-39, excerpt from MS6 6001734-6001868); Exhibit 27 (MS6 6001073-83, excerpt from MS6 6001047-6001123), Microsoft North America FY 96 Business Reviews, 6/96.*

[9]APIs are the industry term for Application Programing Interfaces, which are the bits of operating system code through which applications communicate with the operating system and through the operating

4/4/96 ("Windows won the desktop OS battle because it had more applications earlier than any other platforms."). In turn, Windows' huge installed base compels software developers to develop applications for Windows first, and often for Windows exclusively, refueling the positive feedback loop.[10]

(3) Microsoft Uses Its Monopoly Power To Exercise Leverage Over OEMs

Because of Microsoft's monopoly power, customers expect to receive Windows with the PCs they buy and, therefore, OEMs see no choice but to ship PCs with Windows.[11] Even IBM, which makes its *own* competing operating system, has chosen to preinstall Microsoft's operating system rather than its own on all of its consumer PCs. *Kozel Dep., p. 11, lines 5-24.*

OEMs recognize that their dependence on Windows gives Microsoft substantial leverage over them. As one executive at a major PC OEM put it: "They have established a dominant market share position in the marketplace where we distribute our products, and there's really no option or choice to Microsoft products in these areas." *Von Holle 9/97 Dep., p. 37, lines 11-15*. An executive of another major OEM wrote to Microsoft: "If we had a choice of another supplier, based on your actions in this area, I assure you [sic] would not be our supplier of choice." *Romano Dep., p. 49, line 15 - p. 50, line 3*. Of course, as the executive later testified, "absolutely there's no choice," *Id. at p. 50, line 7.*

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system to the computer. Applications developers write their programs to a specific operating system's APIs. If they want their programs to function on different operating systems, developers must rewrite their code (or "port") their applications to different operating systems. Microsoft writes its APIs to ensure the greatest degree of compatibility between different versions of its own Windows operating systems. No new entrant could develop a new operating system that would be generally compatible with existing Windows applications without either a license from Microsoft or immense reverse engineering efforts that are almost sure to be obsolete by the time they are finished. *Exhibit 30 (MS7 007548), J. Kempin 12/17/97 e-mail*.

[10]*E. Salem Deposition Transcript Excerpts ("Salem Dep."), p. 21, lines 2-18, p. 23, line 22 - p. 24, line 9; E. Dunn Deposition Transcript Excerpts ("Dunn Dep."), p. 10, line 11 - p. 13, line 17; B. Hankins Deposition Transcript Excerpts ("Hankins Dep."), p. 11, line 18 - p. 12, line 18, p. 13, lines 7-22*.

[11]*Browning Decl., ¶ 4-11; Jerry Kozel Deposition Transcript Excerpts ("Kozel Dep."), p. 10, line 5 - p. 12, line 6; Ransom Dep., p. 10, line 5 - p. 11, line 14; Von Holle 9/97 Dep., p. 8, line 2 - p. 10, line 18, p. 12, line 22 - p. 14, line 2; S. Decker Deposition Transcript excerpts ("Decker Dep.,"), p. 10, line 5 - p. 11, line 21; Romano Dep., p. 49, line 15 - p.52, line 6.*

(4) Windows 98 Will Perpetuate Microsoft's Monopoly Power

Windows 98, the successor to Windows 95, will become the dominant operating system for new shipments upon its release, particularly in the OEM channel. Because customers demand not only Windows, but the latest versions of Windows, *Decker Dep., p.11, line 22 - p. 12, line 16,* OEMs will have no commercially viable alternative to Windows 98. *See ibid.; Ransom 10/97 Dep., p.11, lines 4-19; W. McKinney Deposition Transcript Excerpts ("McKinney Dep.), p.12, lines 1-8.* Because Windows 98 will be compatible with Windows 95 applications, it will immediately inherit the huge and commercially critical base of available software programs for users to run on it.

ii. *Microsoft Recognizes That Competing Internet Browsers Pose A Threat To Its Windows Monopoly*

As Microsoft's top executives recognize, Internet browsers[12] and related technologies represent the most serious existing or potential threat to Microsoft's continued dominance of the PC operating system market. Like Windows, the browser products produced by Netscape contain application programming interfaces that enable ISVs to write software applications or "plug-ins" to the browser. In this sense, the Netscape browser is an alternative platform to which software applications can be written. The Netscape browser works on numerous operating systems without having to have the applications' developers go through the time and expense of "porting" (*i.e.*, rewriting) the application for different operating systems. One particular way in which a browser with a large number of users can become an alternate platform for application development is for it to be combined with Sun Microsystems' cross-platform programming language, Java. Java enables applications to run on any platform or operating system, as long as they are written in Java and run on a Java Virtual Machine (JVM). Non-Microsoft browsers,

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[12]In agreements with various firms for the distribution and promotion of its Internet Explorer, Microsoft defines "browser" as

> software and related technology for any Platform that . . . is designed to view, render, browse, hear or otherwise interact with Content on the Internet, the web and/or other public networks now existing or hereafter create.

Exhibit 31 (TWDC 0704-0155), Disney Online Active Desktop Marketing and Distribution Agreement §1.31; Exhibit 32 (AOL-0000145-73), AOL Active Desktop Marketing & Distribution Agreements §1.28.

including Netscape Navigator, serve as the distribution package and host for a cross-platform JVM.[13] *Maritz Dep. Tr. at p. 175, line 18 - p. 178, line 25.*

The widespread distribution of alternative APIs and cross-platform JVMs threaten the very source of Microsoft's monopoly. The more applications written directly to the browser or the JVM that it hosts, the more fungible the underlying operating system becomes. Because browsers such as Netscape Navigator are cross-platform (that is, they will run on any operating system, not just Windows) and have the ability to host cross-platform applications, they pose a significant threat to Windows. *See, e.g., B. Tierkel Declaration, ¶¶ 4-9; P. Backes Declaration, ¶¶ 3-8; Fisher Decl. ¶ III.B.* With a browser running on a computer and applications interacting directly with the browser, the underlying operating system could become less important. In that event, Windows' monopoly power would diminish, or perhaps ultimately be ended altogether.

As early as 1995, Bill Gates recognized the threat Netscape posed: "They are pursuing a multi-platform strategy where they move the key API into the client to commoditize the underlying operating system." *Exhibit 2 (MS6 5004549-4558).* Over the past three years, numerous Microsoft executives have reiterated concerns about the threat posed by competing browser products:

- Brad Silverberg, for instance, wrote that "The Internet Battle" is "not about *browsers.* Our competitors are trying to create an alternative *platform* to Windows. . . ." *Exhibit 33 (MS6 6005550-54)* (emphasis in document);
- Jeff Raikes, Microsoft's Group Vice President for North America sales, lamented the infiltration of "competition" from Netscape into what he colloquially referred to as

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[13]A Java Virtual Machine translates programs written and compiled in the Java programming language into instructions understood by the specific computer CPU on which the JVM is running. Order Re Sun's Motion For Preliminary Injunction, *Sun Microsystems, Inc. v. Microsoft Corporation,* slip op. at 1, C-97-20884-RMW at 2 (N.D. Cal. Mar. 24, 1998,). Therefore, a JVM is needed for each computer CPU on which a Java program is run. *Id.* Microsoft has designed its own implementation of Java technology to be partially incompatible with Sun's cross-platform standards. *See id* at 4-5. In granting Sun a preliminary injunction against Microsoft's use of the Java trademark with Microsoft's incompatible technology, the district court found: "Microsoft's manipulation of the ambiguities surrounding [its Java license agreement] . . . cannot be reconciled with the purpose of [the license agreement] and the Java technology itself. Microsoft's reading of the [license agreement] would essentially allow Microsoft to destroy the cross-platform compatibility of the Java programming environment." *Id.* at 9.

Microsoft's "*Windows Paradise*" and warned: "The situation is threatening our operating systems and desktop applications share at a fundamental level." *Exhibit 34 (MS6 6012713-2718).* Mr. Raikes also declared: "Netscape pollution must be eradicated." *Ibid.;*

- Paul Maritz, Group Vice President for Platforms and Applications, in a presentation on "Internet Browsers" and "How We Win," emphasized that "Netscape/Java is using the browser to create a 'virtual operating system,'" and asked whether Windows will become "devalued, eventually replaceable?" *Exhibit 35 (MS6 6008247-8282)*; and
- Brad Chase recognized that there was a potential danger that a competing Internet browser could eventually "obsolete Windows." *Exhibit 15 (MS7 004127-47).*

Microsoft executives have continued to acknowledge Netscape as a threat to its Windows operating system dominance. For example, Joachim Kempin, Microsoft's Senior Vice President for OEM Sales, pointed out that wide distribution of competing browsers might cause customers to "not know if they are on a UNIX machine, on a Macintosh, or a Windows machine anymore. Because the next browser might have a totally different interface, and it just can't be in our interest to promote that other interface." *Kempin 10/97 Dep., p. 44, lines 20-23.* Similarly, Paul Maritz, Group Vice President for Platforms and Applications, explained how Netscape Navigator posed a threat to Windows by being a major distribution vehicle for the Sun JVM. *Maritz Dep., p. 175, line 18 - p. 178, line 23.* Senior Vice President Jim Allchin, the executive in charge of Windows 98 development, explained that Netscape Navigator threatens to make it "trivial" to replace Windows by creating "a layer that hides the APIs of Windows." *J. Allchin Deposition Transcript Excerpts (Allchin Dep.), p. 125, line 3 - p. 126, line 16.*

At this juncture, it is clear that non-Microsoft browsers remain a threat to Microsoft's operating system monopoly. Microsoft perceives browsers as a threat; Netscape, by both continuing to develop and widely distribute browser technology as an application platform and as a host for Java, continues to threaten to provide competitive alternatives to Windows; and application developers continue to see promise in a browser-based, cross-platform programming environment.

iii. *Microsoft's Anticompetitive Conduct Violates Sections 1 And 2*

In reaction to the threat posed by non-Microsoft browsers, Microsoft has engaged, and

plans to continue to engage, in a variety of exclusionary and predatory practices to protect its operating system monopoly.

(1) Microsoft Has Unlawfully Tied Internet Explorer To Windows

Section 2 prohibits a firm from "wield[ing]" its monopoly power "to tighten its hold on the market." *Berkey Photo, Inc. v. Eastman Kodak Co.*, 603 F.2d 263, 275 (2d Cir. 1979), *cert. denied*, 449 U.S. 1093 (1980). "A variety of techniques may be employed to achieve this end -- predatory pricing, lease-only policies, and exclusive buying arrangements, to list a few." *Id.* at 274. Tying arrangements are another. By using monopoly power to compel a customer to purchase a product it might prefer to purchase elsewhere, a monopolist "forecloses competition on the merits in a product market distinct from the market for the tying item." *Jefferson Parish Hosp. Dist. No. 2 v. Hyde*, 466 U.S. 2, 22 (1984). "By doing so, the [monopolist] may build a strong position in [the tied product market]; and *that position* [in the tied product market], in turn, may increase its power" in its monopoly product. *Grappone, Inc. v. Subaru of New England, Inc.*, 858 F.2d 792, 795 (1st Cir. 1988).

Microsoft's use of its monopoly power in Windows 98 to coerce OEMs to license Internet Explorer implicates precisely this core Section 2 concern. By compelling OEMs to license Internet Explorer with Windows 98, Microsoft will continue to foreclose competition in a separate market -- the market for Internet browsers. Because of the threat that browsers pose to Microsoft's PC operating systems monopoly, this foreclosure of competition on the merits serves to maintain Microsoft's monopoly power. As the Supreme Court has stated, it is unlawful for a monopolist to "employ[] market power as a trade weapon against . . . competitors." *Griffith*, 334 U.S. at 107 (1948); *see also ibid.* ("[T]he use of monopoly power, however lawfully acquired, to foreclose competition, to gain a competitive advantage, or to destroy a competitor, is unlawful.").

Although Microsoft will bundle Internet Explorer with Windows 98, it has gone well beyond linking the two products together. Indeed, it has contractually restrained its OEM licensees -- the conduits through which most copies of Windows are distributed -- from separating the two products. These agreements in and of themselves violate Sections 1 and 2 of the Sherman Act.

Microsoft's contracts prohibit OEMs from "modify[ing] or delet[ing] any aspects of the

Product software" licensed pursuant to Windows 95 (and Windows 98) license agreements. *See infra*, section IV.A.3(c). Microsoft has previously made clear that these licensing restrictions require OEMs to ship Internet Explorer with Windows 95, *see Kempin 10/97 Dep., p. 16, lines 10-22,* and OEMs likewise will not have the freedom under their license agreements to remove Internet Explorer from Windows 98.[14] *See J. Kempin 3/98 Deposition Transcript Excerpts ("Kempin 3/98 Dep.), p. 36, line 12 - p. 37, line 8.* Based on their understanding of the Windows 95 license agreements, OEMs recognize that they are not permitted to remove Internet Explorer.[15] *See, e.g., Kies Dep., p. 9, line 21 - p. 10, line 5; Von Holle 9/97 Dep., p. 14, lines 3-24; Exhibit 18, Gateway 2000, Inc. 9/19/97 Answers to Interrogatories, p. 8*. Similarly, they understand that Microsoft will not permit the removal of Internet Explorer from Windows 98. *See, e.g., Kies Dep., p. 14, line 25 - p. 15, line 5*.

(2) Microsoft's Forced Licensing of Internet Explorer Injures Competition

The effect of Microsoft's tying of its Internet browser to Windows 98 will be, as it was with Windows 95, to impair competition on the merits in the market for Internet browsers[16] and thereby significantly to reduce the major threat to Microsoft's dominance of the operating system

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[14]OEMs have sought in the past to remove icons or other means of access (*e.g*., entries in the "Start" menu or on tool bars) to Internet Explorer. From the end user's perspective, doing so effectively removes Internet Explorer. To the extent a product functions and is designed to function as an application available to end users, removing the means of accessing it unquestionably "removes" the application. Indeed, Microsoft has referred to the "removal" of Internet Explorer in exactly this context in earlier proceedings before the Court and in its own documents. *See D. Cole (1/14/98 am) Hearing Tr., pp. 1681-84; Exhibit 88, Removing IE 4.0 for Win 95 using ieremove.exe.*

[15]Pursuant to the Stipulation and Order entered by the Court on January 22, 1998, Microsoft is now precluded from enforcing this requirement. Under the Order, OEMs are permitted to remove Internet Explorer (as Microsoft defines "remove" in the Add/Remove utility) from Windows 95. At least one OEM has stated its intention to act on this freedom, *see J. Kies Deposition Transcript Excerpts ("Kies Dep."), p. 10, line 12 - p. 11, line 22*, and its interest in having such freedom for Windows 98. *Id. at p. 15, lines 6-8.* Another has undertaken engineering work to configure its PCs to enable end users to choose a browser, a process that would include having Internet Explorer automatically removed if the user selected Netscape Navigator. *See Brownrigg Dep., p.29, line 19 - p.31, line 20.*

[16]As explained below with respect to Section 1 (*see infra*, section IV.B.1(a)), operating systems (including Windows) on the one hand, and Internet browsers (including Internet Explorer), on the other, occupy distinct product markets.

market. Where, as here, products in the tied product market are potential "partial substitutes" for the tying product, antitrust concerns about anticompetitive effects are heightened because tying agreements not only reduce competition in the tied market, but also reinforce market power in the tying market. *See, e.g.*, 10 Areeda et al., Antitrust Law ¶ 1747 a-c, at 230-33 (1996).

The economic consequences of tying arrangements are straightforward. Customers, if compelled to obtain a particular product from a monopolist, are unlikely to obtain a competing product from the monopolist's rival, even if they would otherwise have preferred to do so. *See Jefferson Parish*, 466 U.S. at 12. This is true with Internet browsers as with other products. Many OEMs who are contractually required to preinstall Internet Explorer along with Windows will not preinstall another browser on the PCs they sell because, among other reasons:

- OEMs believe that too many icons and layers cause customer confusion, which could increase product support costs.[17]
- Even without confusion, OEMs bear the burden of providing technical support for the Microsoft software they preinstall, a fact that creates a natural disincentive for preinstalling duplicative titles in a single product category. *See McKinney Dep., p. 27, lines 9-18; Frank Santos Deposition Transcript Excerpts ("Santos Dep."), p. 21, lines 13-25.*
- The preinstallation of two browsers would double the necessary product testing.[18]

Indeed, Microsoft's Senior Vice President of OEM Sales noted that OEMs "should be" wary of installing two browsers on their machines. *Kempin 10/97 Dep., p. 31, lines 13-17.* "If the OEM wants to install the other browser, he can do it. And it's just a matter of how much cost he is willing to have. Because he will probably *have to test all our product first* then he has to test the other products . . ." *Kempin 10/97 Dep., p. 34, lines 13-17 (emphasis added).* Using this argument, Microsoft has actually dissuaded some OEMs from shipping another browser because Microsoft's browser is already on the machine:

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[17]*See Kempin 3/98 Dep., p. 83, line 19 to p. 84, line 13; Ransom 3/98 Dep., p. 27, line 23 - p. 29, lines 8-19, McKinney Dep., p. 27, line 9 - p. 28, line 18; Brownrigg Dep., p. 34, lines 3-11.*

[18]*Kempin 10/97 Dep., p. 32, line 13 - p. 33, line 8; McKinney Dep., p. 27, line 9 - p. 28, line 18; Decker Dep. Tr. at 16-17, 22.*

> Q: . . . [D]oes Microsoft sometimes essentially make this argument to [OEMs]: Why do you need to incur the extra testing costs and the extra user education and maybe undergo the longer loading time --
>
> A: I believe we have.
>
> Q: Is that sometimes successful in persuading OEMs that they don't really need to distribute another browser because they already have Internet Explorer?
>
> A: That is sometimes successful.

Kempin 10/97 Dep., p. 37, lines 10-19.

Because a user's first experience with software is determined by what comes preinstalled on his computer, *see, e.g., Von Holle 9/97 Dep., p. 23, line 14 - p. 24, line 7; Ransom 3/98 Dep., p. 11, line 12 - p. 12, line 3,* distribution through the OEM channel provides Microsoft a significant opportunity to distort users' software choices. As Microsoft's Joachim Kempin has admitted, this is precisely why tying Internet Explorer to Windows forecloses competitive opportunities for non-Microsoft browsers:

> It's known that if people have just one browser on a PC, they would probably at least start out with it. If they decide to go to another one, they would probably -- and they can easily do that, I can't control that. But maybe I can give them the original experience at least once. *Kempin 10/97 Dep., p. 38, line 22 - p. 39, line 2.*

Microsoft also recognizes that competing browsers are significantly foreclosed by its tying of IE to Windows. *See Exhibit 36 (MS7 1033-48), 1/14/97 Presentation (explaining that for Windows 98, priority "#1 is to build IE4 share via OEM distribution").* Distribution of browsers through preinstallation on PCs has been one of the two most significant avenues through which computer users obtain their browser. *Myhrvold Dep., p. 43, lines 7-18; see, e.g., Exhibit 37 (MS7 006063), K. Mehta 3/27/97 e-mail* (25% of IE users obtained it with their computer). As a result, internal Microsoft documents leave little doubt that the foreclosure of competing browsers caused by the forced distribution of Internet Explorer with Windows -- rather than any possible improvement of Windows that might be thought to result from the bundling of the two products -

- is a critical factor in Microsoft's effort to win the browser war:

> Most of IEUs [focus group] were Navigator users. They said they would not switch, would not want to download IE4 to replace their Navigator browser. However, once everything is in the OS and right there, integrated into the OS, in their face so to speak, then they said they would use it because there would be no more need to use something "separate." The stunning insight is this: To make then switch away from Netscape, we need to make them to upgrade to Memphis. . .
>
> It seems clear that it will be very hard to increase browser market share on the merits of IE 4 alone. It will be more important to leverage the OS asset to make people use IE instead of Navigator.

Exhibit 23 (MS7 004343), C. Wildfeuer 2/24/97 e-mail. As Microsoft's Megan Bliss wrote:

> I thought our #1 strategic imperative was to get IE share (they've been stalled and their best hope is tying tight to Windows, esp. on OEM machines). That is, unless I've woken up in an alternate state and now work for Netscape.

Exhibit 38 (TXAG 0009634), M. Bliss 3/25/97 e-mail re: *Closure on Memphis action items from 3YO and Billg Memphis review.* Internal Microsoft presentations assessing Microsoft's competitive advantage against Netscape list the "huge OEM channel advantage" and note that Microsoft "own[s] the client OS." *Exhibit 39 (MS6 6012195), Developer Relations Group Public Internet Plan (draft version 0.975).* As Carl Stork makes clear, Microsoft used its "OEM channel advantage:" "Browser Share is Job 1 at this company, and OSR2 [a version of Windows 95 distributed by OEMs] is the vehicle to get IE3 onto these machines." *Exhibit 40* (*MS0009363A)*.

Given the importance of the OEM channel for browser distribution, Microsoft's tying of Internet Explorer to Windows has had, and will have, a significant anticompetitive effect. Moreover, as discussed below, this effect is not limited to substantial foreclosure of competitive opportunities to distribute non-Microsoft browsers on new PCs. It also reinforces and augments the anticompetitive effects of Microsoft's other exclusionary conduct.

(3) Microsoft Has Unlawfully Injured Competition By Imposing On OEMs Windows' "Boot-Up" And "Default Screen" Restrictions

As a condition of licensing Windows 98, Microsoft has prohibited OEMs from adding to the sequence of screens every user sees when first turning on a new PC with Windows preinstalled (the "boot-up" sequence) and from modifying the default "desktop" screen (or "user interface") displayed to the user when the PC is first turned on.[19] OEMs cannot remove folders or icons from the Windows desktop, cannot create icons or folders larger than those placed by Microsoft on the desktop, and cannot alter the boot-up sequence by, for instance, presenting an OEM-created screen or "shell" that would highlight a choice of Internet browsers or the OEM's own Internet offerings. Microsoft's restrictions mean that virtually every new PC will present the same screens and the same set of Microsoft-dictated software -- including Microsoft's browser -- to new users when they first turn the machine on, regardless of which OEM built it and what other choices that OEM wanted to make.[20]

The Microsoft desktop screen and boot-up sequence restrictions produce several anticompetitive effects that significantly impede the successful distribution of competing browsers in the most important channels for getting browsers to end users. First, by barring OEMs from removing all or part of Microsoft's browser product, the restrictions provide the mechanism

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[19]The original Windows 95 licenses stated that OEMs may not "modify the Product software [or] delete or remove any features or functionality without the written approval of MS in each instance." *See, e.g., Exhibit 41 (MSV 0000163), Microsoft OEM License Agreement for Desktop Operating Systems, Exhibit C1.* Subsequent amendments to Windows 95 license agreements have made the prohibition clearer: "COMPANY is not licensed to, and agrees that it will not, modify, in any way, or delete any aspect of the Product software (including, without limitation, any features, shortcuts, icons, 'wizards', folders (including sub-folders) or programs of Product software) as delivered by MS in the Product Deliverables, except if and as specifically permitted below in the OPK User's Guide ('OPK') provided in the Product Deliverables." *See, e.g., Exhibit 41 (MSV 00203-04), Amendment 7 to Microsoft OEM License Agreement for Desktop Operating Systems; OEM Preinstallation Kit (OPK) for OEM Service Release 2. See Exhibit 93 DOJ 00049.* Microsoft's Windows 98 license agreements contain similar or identical restrictions. *See Exhibit 42, Windows 98 license agreement, ¶ II(E)(iii), Exhibit C (Additional Provisions Key 18(I)).*

[20]Although the restrictions technically apply only to modification of the Windows startup sequence the first time the PC is turned on, and technically permit OEMs to engineer a mechanism for "user-initiated" action after boot-up is complete to alter the Microsoft-required screens, these factors are of negligible value to OEMs. It is both costly and time-consuming for OEMs to develop such a mechanism. *See, e.g., Exhibit 43 (MSV 9136A-9139A), B. Chase 3/1/96 e-mail* ("most OEMs won't go through the hassle to develop such a DOS utility"); *J. Kempin 3/98 Dep., p. 62, line 2 - p. 63 line 10; R. Brownrigg Dep., p. 49, line 15 - p. 51, line 2; F. Santos Dep., p. 29, line 11 - p. 30, line 15.*

Microsoft uses to enforce its tie of Internet Explorer to Windows.

Second, the restrictions deprive PC OEMs of the freedom to configure their computers in a way that presents or positions competing software products more prominently than Microsoft's bundled (and contractually non-removable) products such as Internet Explorer. By using its monopoly power simultaneously to require both preinstallation and unrivaled positioning of its browser, Microsoft effectively ensures that no competing browser can ever receive better placement or treatment on any PC.

Moreover, users are particularly likely to select the Internet services they will use (including browsers and their choice of ISP's) the first time they turn on the PC:

> In order to protect our position on the desktop and increase the likelihood that IE gets the prominent position with the end user we should move the Sign Up Wizard into the boot-sequence somewhere, before we give control over to the OEM. This way we can increase the likelihood that an end user gets the option to sign up for solutions that promote IE before they get into the desktop or any customized shell that features other browser solutions. *Exhibit 43 (MSV 9136A-9139A), B. Chase 3/1/96 e-mail.*

Microsoft has done just this, moving its Internet Connection Wizard into the Windows 98 startup sequence. Both Microsoft's executives and others in the industry expect that the Internet Connection Wizard will become an even more important means by which users select their ISP or OLS, and thus often their browser, than it was in Windows 95. *See, e.g., B. Chase Dep., p. 184, line 13 - p. 185, line 6; J. Allchin Depo., p. 83, line 15 - p. 86, line 22; D. Colburn Deposition Transcript Excerpts ("Chase Dep."), p. 47, lines 9-19.* Microsoft's boot-up sequence and screen restrictions, of course, deny OEMs similar freedom to create a more "prominent position" for non-Microsoft browsers.

Indeed, more generally, Microsoft's screen restrictions block OEMs from entering into innovative partnerships with non-Microsoft software vendors to provide new or different software options and interfaces to consumers. This thwarts OEMs' abilities to differentiate their products by highlighting competing Internet software or service offerings, as they did before Microsoft imposed its screen restrictions. For example, one major OEM would like the flexibility to give its customers a choice of Internet access providers as part of the PC boot-up sequence, *see Exhibit*

44 (GW 026420-24); *R.. Brownrigg Dep., p. 41, line 1 - p. 44, line 22, p. 49, line 5 - p. 51, line 2; J. Von Holle 4/98 Dep., p. 13, line 3 - line 25,* and in the process offer those users a choice of browsers when they register with the selected service. *Brownrigg Dep., p. 49, line 15 - p. 50, line 13; J. Von Holle 4/30/98 Dep., p. 14, line 15 - p. 14, line 22.* In essence, it wishes to define its own Internet software and service partners and arrange direct business relationships with them in order to offer its customers additional options. Microsoft's restrictions, however, have prevented it from meeting what it perceives to be consumer demand. Other OEMs have been similarly thwarted from offering users similar choices of software and services during the boot-up sequence. *See, e.g., McKinney Dep., p. 14, line 12 - p. 15, line 24, p. 19, line 17 - p. 21, line 19; Romano Dep., p. 40, line 21 - p. 43, line 18.*

Microsoft will continue to deny this basic OEM and consumer choice when it releases Windows 98. OEMs already have requested that Microsoft give them flexibility to highlight their own competitive offerings, but Microsoft has made clear it intends to continue to impose and enforce its screen restrictions.[21] *F. Santos Dep., p. 19, line 11 - p.20, line 13; J. Von Holle 4/30/98 Dep., p. 14, line 23 - p. 15, line 24*.

Internal Microsoft documents written before it imposed the restrictions amply illustrate the OEM choice that Microsoft feared -- and that it eliminated through the boot-up and screen restrictions. For example, Microsoft CEO Bill Gates wrote of his concern that OEMs were bundling non-Microsoft browsers and "coming up with offerings together with Internet Service Providers that get displayed on their machines in a FAR more prominent way than . . . our Internet browser" and that those offerings were interfering with the "very very important goal" of "[w]inning Internet browser share." *Exhibit 45 (MSV 9445A), 1/5/96 B. Gates e-mail*. At the same time, Group Vice President Paul Maritz reported to Mr. Gates that ISPs (which at that time did not generally distribute Internet Explorer) were already included in OEM shells (*i.e.*, OEM-created screens that provide access to applications) that were "invariably positioned on the

[21]In Windows 98, OEMs will be allowed to place their own ISP offerings within the Microsoft Internet Connection Wizard; however, the choice of those offerings, as described below, will be conditioned on ISP agreement to Microsoft's restrictions on their promotion and distribution of non-Microsoft browsers. Furthermore, OEMs must pay Microsoft for the privilege of including their own offerings in the Internet Connection Wizard.

desktop more strongly by our OEMs than any Microsoft offering." *Exhibit 46 (MSV 0009360A-61A), Paul Maritz 1/6/96 e-mail to Bill Gates.* Microsoft's screen restrictions eliminate these opportunities for competing browsers and Internet Services because they "protect [Microsoft's] position on the desktop."

As will be seen below, Microsoft's ability to prevent OEMs from deleting or overshadowing its products allows Microsoft to assure IAPs, ICPs, and ISVs that, if they agree to exclude and foreclose competing browsers from their services and products, Microsoft will provide them distribution and favorable promotion on every Windows desktop -- an offer few ignore. *See, e.g., R. Brownrigg Dep., p. 54, line 19 - p. 57, line 15.*

(4) Microsoft Has Entered Into Exclusionary Contracts With Internet Service Providers and Online Services

Microsoft has entered into agreements with the largest and most important ISPs and OLSs (sometimes collectively called Internet Access Providers, or "IAPs"), including America Online, CompuServe, Prodigy, and MCI, that exclude rival Internet browsers from the single most important browser distribution channel.

(a) Microsoft's Agreements Expressly Restrict The Ability Of IAPs To Distribute Competing Browsers

Microsoft has entered into a series of contracts with nearly all the nation's leading IAPs for placement of access to their services in two places on the Windows desktop: the Internet Connection Wizard ("ICW") and the Online Services Folder. These agreements are exclusionary: They expressly and significantly restrict consumers' access to, and even their ability to be told about, non-Microsoft browsers that their service providers might otherwise distribute and promote.[22] These contracts have the purpose and effect of excluding the Netscape Navigator browser from distribution through the vast majority of U.S. IAPs, which are the single most important channel through which users acquire their browsers. In particular, the agreements require that:

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[22] *See, e.g., Exhibit 47 (MS6 5001199-1945) License and Marketing Agreement between AOL and Microsoft ("AOL Agreement) § 7; Exhibit 48 (MS6 5000168-89), Promotion & Distribution Agreement between CompuServe and Microsoft ("CompuServe Agreement") § 3; Exhibit 50 (MS6 5001127-1151), Spry Agreement Exhibit B, ¶ 5.*

- IAPs must market, promote and distribute Internet Explorer as the "exclusive" or "primary" browser, and cannot distribute a non-Microsoft browser unless it is specifically requested by the customer;
- IAPs may not "express or imply" to a customer that another browser is available;
- Even if a customer specifically requests a competing browser, Microsoft requires IAPs in the Referral Server to ship Internet Explorer as the only browser a large majority of the time, usually for at least 75% to 85% of all browser shipments.[23] The providers in the Online Services folder must ship Internet Explorer, and no other browser, at least, 85% of the time;[24] and
- IAPs, with minor exceptions, cannot advertise or promote any non-Microsoft browsers.

While Microsoft has recently announced, after coming under intense scrutiny and on the eve of likely antitrust enforcement action, that it will waive some of the restrictions for ISPs, the most exclusionary restrictions remain for the most important IAPs -- the OLSs, including AOL, CompuServe, and Prodigy.[25]

(b) IAPs Agree To Microsoft's Demands In Order To Gain

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[23]*See, e.g., Exhibit 47 (MS6 5001199-1245), License and Marketing Agreement between America Online ("AOL") and Microsoft ("AOL Agreement"), § 7; Exhibit 48 (MS6 5000168-89), Promotion & Distribution Agreement between CompuServe and Microsoft ("CompuServe Agreement"), § 3.1 - 3.3; Exhibit 51 (MS6 5000920-47), Internet Sign-Up Wizard Referral and Microsoft Internet Explorer License and Distribution Agreement with Mindspring Enterprises, Inc. ("Mindspring Agreement") §3.1, Exhibit C.*

[24]*Exhibit 47 (MS6 5001199-1245), AOL Agreement § 7; Exhibit 48 (MS6 5000168-89) CompuServe Agreement § 3.3(b); Exhibit 49 (MS6 5000997-1019), Promotion & Distribution Agreement between Prodigy and Microsoft ("Prodigy Agreement") §3 (MS6 5000997-1019).*

[25]Microsoft is not waiving restrictions for firms that appear in the Online Services folder. *Chase Dep., p. 173, lines 8-17; Colburn Dep., p. 59, line 12 - p. 61, line 18.* Those restrictions substantially impair competition among browsers because the affected OLSs -- America Online, CompuServe, Prodigy, AT&T WorldNet and MSN -- represent over 53% of the total North American subscriber base for Internet access *Exhibit 52 (MS7 000591), 1/23/98 Internet Customer Unit FY '98 Mid-Year Review*. Moreover, the Microsoft Vice President who oversees the ISP arrangements has testified that even the ISPs in the referral server whose restrictions Microsoft purported to waive will still be prohibited from distributing and promoting other browsers on any greater or more prominent basis than Internet Explorer. *C. Myhrvold Dep., p. 109, line 6 - p. 112,* line 12; *p. 119, line 6 - p. 120, line 2; p. 122, lines 7-9; p. 176, lines 1-12.*

Windows Desktop Placement

Microsoft is able to induce IAPs to enter into these restrictive agreements as a condition of the IAPs' placement on the Windows desktop, which is an unusually attractive distribution and promotional mechanism for software providing access to IAP services.[26] As Brad Silverberg, former head of Microsoft's Internet Group, told AT&T during negotiations:

> You want to be part of the Windows box [desktop], you're going to have to do something special for us. There are very, very few people we allow to be in the Windows box. If you want that preferential treatment from us, which is extraordinary treatment, we're going to want something very extraordinary from you.

Silverberg Dep., p. 159, lines 10-16. The "something very extraordinary" Microsoft was demanding was exactly what the United States here challenges: an explicit agreement to restrict the distribution, advertisement, promotion, or even mention of non-Microsoft browsers.[27]

Few facts illustrate the critical importance to Microsoft of gaining preferred or exclusive distribution for Internet Explorer better than Microsoft's decision to place AOL on the Windows desktop. AOL was and is the fiercest competitor to Microsoft's own online service, MSN, on which the company had already spent many millions of dollars and given a preferred position on the Windows 95 desktop. Bill Gates initially strongly opposed giving AOL access to the Windows desktop, stating that doing so would be tantamount to "putting a bullet through MSN's head." *Silverberg Dep., p. 187, lines 2-7.* Nevertheless, Gates and other top Microsoft executives decided to place AOL in the Online Services Folder.

Microsoft's motivation for such an extraordinary step was clear: trade the attractiveness of access to the Windows desktop for AOL's agreement to distribute Internet Explorer essentially

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[26]Indeed, Cameron Myhrvold, Microsoft's executive in charge of overseeing its relationships with ISPs, has since confirmed that Microsoft specifically *created* the Internet Connection Wizard in part to induce ISPs to distribute Internet Explorer as the "preferred" browser. *C. Myhrvold Dep., p. 64, line 11 - p. 65, line 20; p. 68, lines 20-23.*

[27]The payment with which Microsoft extracted these exclusionary agreements was access to an attractive distribution vehicle. However, the agreements would have been equally anticompetitive had Microsoft simply paid the IAPs and ICPs with the anticipated monopoly profits it obtains from the agreements' exclusionary effects.

exclusively to its millions of users.[28] Indeed, nearly all significant U.S. IAPs have agreed to the exclusionary restrictions, in many cases because doing so was Microsoft's "price" for access to the Windows Microsoft desktop. *See, e.g., K. Knott Deposition Transcript Excerpts ("Knott Dep."), pp. 14, 21-22; D. Colburn Dep., p. 29, line 4 - p. 30, line 6; p. 33, lines 14-21; p. 33, line 14 - p. 34, line 23.*

Significantly, these IAPs agreed to exclude Netscape and other browsers despite their preference not to be locked into exclusive or near-exclusive browser distribution arrangements. For example, CompuServe, the nation's second largest OLS, preferred "to have flexibility in software" that it distributes, but nevertheless agreed not to ship, market, or physically distribute any non-Microsoft browser with its online service and branded services unless expressly requested by a customer, and not to distribute more than a small percentage of non-Microsoft browsers even upon a customer request. *K. Knott Dep., p. 21, line 6 - p. 23, line 20; p. 25, lines 4-5.* MCI, a significant ISP, also would have liked to "have had the flexibility to be able to promote other browsers should there be a marketing advantage to do so," *S. Von Rump Deposition Transcript Excerpts ("Von Rump Dep."), p. 11, line 11 - p. 12, line 8,* but it too agreed to restrictions partly as the price of being included in Windows. *Id. at p. 14, line 12 - p. 15, line 14.* Similarly, AT&T executives told Microsoft that it wanted to remain "browser neutral," and that the "level of exclusivity" demanded by Microsoft was problematic for its partnership with Netscape. Nevertheless, AT&T ultimately agreed to Microsoft's restrictions and eliminated browser neutrality in order to gain access to Windows. *Exhibit 58 (MS6 6006096), D. Steele 4/14/96 e-mail; B. Silverberg Dep., p. 159, line 8 - p. 160, line 10; p. 170, line 21 - p. 171, line 5.*

(c) Microsoft's IAP Contracts Injure Competition Among Browsers

Microsoft's exclusionary contracts with IAPs deny its browser competitors access to the most important avenue for browser distribution and promotion. Microsoft has estimated that at

[28]For its part, AOL decided to enter into the restrictive agreement in part because of the value of distribution with Windows. *Colburn Dep., pp. 26-27, 29.* AOL considered Microsoft's control over the operating system market and the fact that "their distribution involved essentially every PC on the marketplace," *id. at pp. 43-44,* and ultimately agreed to such stringent restrictions "[b]ecause that was the price of admission for getting the deal done." *Id. at p. 40.*

least 31% of Internet users get their browsers from an IAP. *Exhibit 53 (MS6 5003741-43), Chase 9/9/96 e-mail. See also Myhrvold Dep. p. 49, lines 3-9 (in 1997, Microsoft estimated this figure at 35%).* As Microsoft's executive in charge of dealing with ISPs recently explained, "it is logical to me that the company providing you with Internet access is a prime place to get the browser from which you do that Internet access." *Id. at 46-49.*

The IAPs that have entered into restrictive agreements as a condition of placement in the Windows Online Services folder -- AOL, CompuServe, Prodigy, AT&T WorldNet, and MSN -- account for the majority of Internet access. In 1997, Microsoft estimated that 43% of home users access the Internet through AOL alone. *Exhibit 54 (MSV 10540-77), April 1997 IE Market Review.* Because the percentage of Internet use via AOL is so high, Microsoft described the deal through which AOL agreed to exclusively use Internet Explorer in its client software as a "coup" and an "opportunity to help establish -- establish a Microsoft platform. . ." *Exhibit 55 (MS6 5003676); Silverberg Dep., p. 124, lines 16-24.*

Microsoft's restrictive agreements injure consumers not only by restricting their choice of browsers but also by limiting the flow of information about competing browsers. Microsoft imposes a gag rule on IAPs by preventing them from expressing or implying to subscribers that an alternate browser is available with their services and by greatly restricting the IAPs' abilities to advertise or promote any non-Microsoft browser.[29] As a result of the contracts, many IAPs no longer mention, or provide users the ability to download, Netscape Navigator. *See, e.g., Stephen Von Rump Depo at p. 10, line 6 - p. 11, line 10.*

Finally, Microsoft offered payment -- both in the form of "reverse bounties"[30] and direct cash incentives -- to secure a high level of exclusivity for Internet Explorer and to convert current

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[29]*See, e.g., Exhibit 50 (MS6 5001138), Spry Internet Sign-Up Wizard Referral Agreement, Exhibit B; Exhibit 56 (MS6 5000862-78), MCI. Addendum D to Internet-Sign Up Wizard Referral Addendum to Strategic Relationship Framework Agreement Exhibit C §§ 6,7; Exhibit 57 (MS6 5000003-28), Earthlink Exhibit C §§6,7.*

[30]The "reverse bounty" came in the form of a discount off referral fees owed to Microsoft for subscribers obtained through the Internet Referral Server. Thus, in order to convert the installed base to Internet Explorer, Microsoft gave up revenue it otherwise would have received. *C. Myhrvold Dep., p. 128, line 11 - p. 129, line 17.*

users of Netscape Navigator. The "reverse bounties," which Microsoft conceded entailed foregoing revenue it otherwise would have received, were offered for what Microsoft termed "competitive upgrades." See, *e.g., Exhibit 50 (MS6 5001140), Spry agreement , Exhibit C,) p. 28; C. Myhrvold Dep. p.128, line 11-p.129, line 4* . Microsoft even offered to pay off AT&T's $17 million minimum commitment to Netscape, in the form of reductions from the bounties AT&T would pay Microsoft for subscriber referrals, in return for a "high level of exclusivity" for Internet Explorer. *Exhibit 58, Dan Steele 3/14/96 e mail (MS6 6006096).* In addition, Microsoft actually gave some IAPs funding in order to switch their installed base to Internet Explorer. *Myhrvold Dep. at p. 129, line 18 - p. 130, line 25.* Thus, Microsoft bought exclusion both indirectly, by using the promise of distribution through Windows, and directly, by paying for it.

(5) Microsoft Has Extracted Exclusionary Contracts From Internet Content Providers And Independent Software Vendors

Microsoft's agreements with ICPs add to the competitive harm that Microsoft's agreements with OEMs and IAPs cause. ICPs provide content that consumers view on the web. In return for the placement of a "channel" button[31] on the Windows desktop, Microsoft's agreements limit ICPs' distribution, support, and promotion of non-Microsoft browsers. As with Microsoft's agreements with IAPs, Microsoft has used its attractive Windows desktop real estate to induce ICPs to agree to exclude its browser rivals

Microsoft's contracts with the largest and most popular ICPs require those ICPs to promote their Microsoft channel exclusively and restrict the ICPs' abilities to deal with "Other Browsers":[32]

- ICPs are not allowed to compensate in any manner a producer of an "Other Browser" --

[31]A "channel" is a feature of the Active Desktop shipped with Internet Explorer 4.0, and soon to be shipped as an interface to Windows 98. Channel buttons are simply branded icons on the Windows desktop screen that, when clicked, lead the user to a particular content provider's site or service. Examples of channels on the Active Desktop include The Disney Channel and a channel developed by Intuit, providing financial software and services.

[32]The definition of "Other Browsers" is limited to the top two browsers (exclusive of Internet Explorer) by browser share.

including by distributing its browser -- for the distribution, marketing, or promotion of the ICP's content, effectively precluding payment for a channel on Netscape's competing Netcaster product;[33]

- Even if an "Other Browser" (namely Netscape) distributes -- without compensation -- an ICP's content through Netcaster, the ICP is still prohibited by its Microsoft contract from promoting or advertising the existence of its Netcaster channel, and from licensing its logos to Netscape in order for Netscape to promote and highlight the existence of that content for Netcaster;[34]
- ICPs are not allowed to promote any "Other Browser" products;
- Microsoft restricts the distribution of "Other Browsers" by requiring that the ICP "distribute Internet Explorer *and no Other Browser* as an integral part" of any ICP Channel Client for the Win32, Win16 or Macintosh platforms,[35] and
- ICPs must create channel content exclusively viewable with Internet Explorer, and optimize many of their websites to take advantage of Internet Explorer-specific extensions to web standards (such as HTML) and Windows-specific technology (such as ActiveX);

In addition to limiting arbitrarily the definition of "Other Browser" to its top two browser competitors, Microsoft has made clear to its ICP signatories that its restrictions are aimed at Netscape. For instance, a Microsoft representative warned HotWired that there should be no Wired branded presence on any Other Browser, and that Microsoft didn't even want to see a Netscape Netcaster press release that mentions the word "HotWired" or even "Wired." *Exhibit 62 (WD000221), Wired's Lisa Gerhauser 6/5/97 e-mail*.

(a) Microsoft Induced ICPs To Enter Into Exclusionary Agreements

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[33] *See, e.g, Exhibit 31, Disney Active Desktop Agreement, §2.4(b); Exhibit 70, ESPN Active Desktop Agreement, § 2.4; Exhibit 59, Hollywood Online Active Desktop Agreement, § 2.4.; Exhibit 60, CNET Active Desktop Agreement, § 2.4*

[34] *See, e.g., Exhibit 31, Disney Active Desktop Agreement, § 2.4; Declaration of Steve Wadsworth, ¶¶ 13-14.*

[35] *See, e.g., Exhibit 61, NBC Active Desktop Agreement § 2.3; Exhibit 32, AOL Active Desktop Agreement §2.4*

As with its agreements with IAPs, Microsoft has been able to secure these exclusionary ICP terms because of its ability to provide ubiquitous distribution through Windows. Microsoft's promotional pitch to some ICPs explicitly spelled out the appeal of incorporation with Windows, which Microsoft called its "crown jewel." *Declaration of Steve Wadsworth ¶ 5; see also Exhibit 63 (SPORT 000086), 5/29/97 "Benefits of becoming a Platinum partner."* Microsoft's own documents even list "Windows distribution -- for IE, and as draw for partners" as a "competitive lever" over Netscape. *See Exhibit 65 (MS6 6003202-3227), Internet Client and Collaboration 3 Year Business Outlook, 2/11/97; see also Exhibit 92 (MS6 000601346*) (key Microsoft assets include placement on the Active Desktop).

One of the major business imperatives of a content provider is to reach the broadest audience possible, and thereby increase the value of its websites to Internet-based advertisers. Nonetheless, many ICPs acquiesced to exclusionary agreements which included requirements that they design websites that would not be viewed as well with Netscape Navigator specifically in order to gain access to the Windows real estate. *See, e.g., Declaration of Steve Wadsworth at ¶¶ 3, 4; Declaration of Harry Chandler at ¶ 5.* As one ICP put it: "The way I've been looking at this is that a preferred position on the active desktop -- which means being bundled into the operating system -- is of *almost incalculable value. . .*" (emphasis added). *Exhibit 67 (ZD 0127), ZDNET's David Shnaider 1/5/97 e-mail.*

(b) Microsoft's ICP Agreements Exclude Competing Browsers And Foreclose Browser Competition

The importance of these contracts to Microsoft is illustrated by the length to which Microsoft has gone to enforce them. For example, Disney was able to carve out an exception that allowed it to have a Netcaster channel (but only on Microsoft's condition that it not compensate Netscape for, or promote the existence of, the channel).[36] Microsoft has demanded that even the Disney logos and characters that Disney wished to appear on Netscape's Netcaster channel bar be removed as a prohibited promotion of Netcaster. Rather than enmesh itself in a legal battle with Microsoft and risk being removed from the Active Desktop, Disney redesigned its Netcaster

[36]*Disney Active Desktop Marketing, Distribution & Promotion Agreement §§ 2.2., 2.3 (TWDC 0369-88).*

channel to have text only.[37] *Declaration of Steve Wadsworth ¶¶ 12-13.* Other content providers, such as Hollywood Online, also did not enter into certain arrangements with Netscape, partly because of restrictive contracts with Microsoft. *Declaration of Harry Chandler ¶ 6.*

Similarly, Intuit, one of the largest ICPs and leading producers of application software in the United States,[38] entered into a contract with Microsoft that prevented it from shipping or promoting Netscape Navigator with Quicken, Turbo Tax, and QuickBooks, its popular and widely used financial software. Microsoft required Intuit to remove all "Netscape Now" buttons for downloading Netscape from many of its top web pages; prevented Intuit from entering into an agreement with Netscape for the promotion of Intuit content in exchange for some economic value; and required Intuit to place "Best Viewed with IE" logos on its home pages; *Exhibit 68 (INT 00001-25), Internet Marketing Distribution and Promotion Agreement §§ 2.2.* Intuit agreed to these anticompetitive terms partly because it felt it was important to be on the Windows desktop. *Dunn Dep., p. 23, line 1 - p. 24, line 1; p. 45, line 23 - p. 46, line 3.*

Absent the agreement, according to its Senior Vice President and Chief Technology Officer, Intuit "would have already entered into an agreement with Netscape to provide financial content on Netscape Web Sites," *Dunn Dep., p. 41, line 15 - p. 42, line 19*, and would have continued to promote Netscape Navigator on its sites. *Id. at p. 39, lines 10-24.* Finally, absent the prohibition on shipping Navigator with its products, Intuit would probably have continued to distribute it with Quicken, as it had done since 1995. *Id. at p. 37, line 17 - p. 38, line 11.*

In addition to the harm to competition caused by Microsoft's distortion of ICPs' dealings with non-Microsoft browser producers, Microsoft's contracts threaten to harm competition by requiring that ICPs adopt certain Microsoft-specific technologies. Rather than allowing the market to determine, based on the merits, which competing standard or technology will prevail,

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[37]Now that Microsoft has waived its restrictions on ICPs, Disney will include its logos and characters on Netcaster. *Steve Wadsworth Declaration ¶ 13.* This is one indication of the extent to which the restrictions skewed market behavior in Microsoft's favor.

[38]Turbo Tax alone accounts for a large number of units sold. 1.7 million units of TurboTax were sold in 1997, and 1.2 million units in 1996. *Exhibit 69, Robert Pfeiffer article, "Titles Make Tax Time Less Taxing: Intuit, block financial, Prepared for New Laws, Electronic Filing This Season," in 2/9/98 Computer Retail Week.*

Microsoft instead requires that ICPs adopt "Active Platform"[39] and design a certain number of their websites with Windows-specific technologies, making those sites less attractive when viewed with competing browsers. *See, e.g., Exhibit 31, Disney Active Desktop Agreement §§2.3, 2.4, Exhibit A; Exhibit 68, Intuit Internet Explorer Marketing, Distribution & Promotion Agreement, Exhibit A.* As Microsoft executive John Ludwig wrote Bill Gates in July 1997:

> We have seen very little adoption of the technology tho [sic]. Finally with ie4 we have our top tier of content partners using the technology (because we force them to in our contracts with them). *Exhibit 72 (MS7 015728), J. Ludwig 7/23/97 e mail*.

Microsoft's ICP contracts threaten to tip the browser battle decisively in Internet Explorer's favor and to eliminate the single most significant threat to Microsoft's operating system monopoly. Accordingly, Microsoft exclusionary agreements with ICPs, which have no legitimate business justification, *see infra,* section IV.A.5(c), constitute an unlawful attempt by a monopolist to insulate its monopoly from competition. *See, e.g,. Lorain Journal Co. v. United States*, 342 U.S. 143, 149 (1951).

iv. *Microsoft's Exclusionary Practices, Particularly Taken Together, Threaten Imminent Anticompetitive Harm*

Even taken individually, each of Microsoft's anticompetitive practices impairs a significant avenue by which consumers obtain non-Microsoft Internet browsers, and by which Microsoft's browser rivals attempt to satisfy the demands of those consumers. But rather than assess each practice separately, the Court should consider their *cumulative* effects in assessing the likelihood of anticompetitive harm under Section 2. *See, e.g., Continental Ore Co. v. Union Carbide & Carbon Corp*., 370 U.S. 690, 699 (1962) (plaintiffs "should be given the full benefit of their proof without tightly compartmentalizing the various components and wiping the slate clean after scrutiny of each").

Considered in this context, Microsoft's conduct has particularly significant anticompetitive effects. It directly forecloses opportunities for non-Microsoft browsers in what Microsoft executives recognize as "the two most important channels for distribution of browsers" -- the

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[39]The Active Platform is a "series of Microsoft specific technologies" that are not accessible by other browsers. *Dunn Dep., p. 43, lines 4-5, 17-20.*

OEM and IAP channels, *see Myhrvold Dep., p. 43, line 7-15* -- and substantially biases other distribution channels (*e.g.*, promotion by ICPs, including downloads from many of the most visited websites in the United States, and bundling with ISV software). Moreover, such other avenues of distribution are becoming less significant over time. Historically, one of the most important methods of distributing browsers other than through IAPs or OEMs is via direct "download" over the Internet. However, Microsoft itself recognizes the decreasing viability of browser distribution through downloads as browsers increase in complexity and, more importantly size, resulting in inordinately long download times and a high rate of failure. *See, e.g., Myhrvold Dep., p. 152, line 19 - p. 153, line 4; J. Belfiore Dep., p. 45, lines 2-16; Exhibit 73 (MS7 004715), B. Chase 11/19/97 e-mail* ("only a little more than half of the people that download the active set-up end up installing the browser. I think they don't figure out what to do once they download the set-up stub")*; Exhibit 20 (MS7 004273), K. Mehta 3/27/97 e-mail* ("Overall 34% of all surfers (not just IE users) have ever downloaded a browser. That means 66% of everybody on the web has never downloaded a browser. . . . Almost 60% of surfers have never downloaded any software from the web. [M]y sense is that these people are not very likely to download anything, let alone a browser that takes 2 hours to download, from the web.") Therefore, with Microsoft moving increasingly aggressively to dominate the OEM and IAP channels, Microsoft's restrictive contracts in the OEM, IAP, ICP and ISV channels threaten even greater foreclosure in the future.

The cumulative impact of Microsoft's conduct is also greater than the sum of its individual parts. Indeed, each practice tends to reinforce the others, making the foreclosure of competition in each channel even more important than it would be if Microsoft had not foreclosed other channels that might otherwise be available to competing browsers. Microsoft's tie of Internet Explorer to Windows, coupled with its restrictions on OEM freedom to prominently feature other browsers, affects not only competition for browser distribution in the OEM channel, but also ripples into the IAP, ICP, and ISV channels by increasing the likelihood that IAPs will deal with Microsoft to secure preferential positioning on PCs (something they can do only by agreeing to license and distribute Internet Explorer) and, in turn, decreases the further availability of

alternative distribution channels for competing browsers.[40] In turn, this skewing of ICP and ISV support for proprietary, programming extensions is likely to affect end user, OEMs' and IAPs' (and ICPs' and ISVs') decisionmaking about browsers by making content designed specifically for IE -- and either not available, or available only in inferior form, to end users who visit the affected websites.

By unreasonably biasing and influencing distribution, investment, and technology standards decisions, Microsoft's conduct, considered in the aggregate, is substantially likely to entrench Microsoft's operating system monopoly and harm competition -- *even if Microsoft does not foreclose all avenues of distribution for competing browsers, and even if Microsoft's conduct does not give it a monopoly position in the browser market* (though there is a dangerous probability this will occur, *see infra*, section IV.C.4). By restricting competition in critical channels of browser distribution, Microsoft's conduct directly reduces the ability of such products to acquire and retain substantial enough distribution and usage to fulfill their promise as application platforms and interfaces to an extent sufficient to pose a competitive threat to Microsoft's monopoly. *See Fisher Decl., ¶ III.D; Sibley Decl., ¶ 52.* Any alternative to the Microsoft operating system platform requires a *critical mass* of consumer usage. Microsoft thus can insulate its monopoly from competition by preventing the browser and Java alternatives from obtaining that critical mass, even if it does not exclude them from the market altogether. Accordingly, Microsoft's conduct, unless restrained by the Court, is substantially likely to enable Microsoft to destroy the incipient browser-based threat to its operating system monopoly.

v. *Microsoft's Exclusionary Conduct Lacks Legitimate Business Justification*

Conduct that excludes rivals and lacks legitimate business justification -- either because it does not advance competition on the merits or because it excludes competitors in an unnecessarily restrictive way -- violates Section 2. *See, e.g., Eastman Kodak Co. v. Image Tech. Servs., Inc.,*

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[40]*See supra*, fn. 21, 25. As noted, Microsoft has announced that it has unilaterally waived restrictions on IAPs in the Referral Server, but that IAPs are still subject to a requirement to distribute and promote Internet Explorer on no less favorable terms than any other browser. Of course, according to Microsoft executives, Online Services that wish to continue to appear in the Online Services Folder will continue to be subject to the full range of Microsoft's exclusionary restrictions. *See, e.g., Colburn Dep., p. 33, line 22 - p. 34 line 23; Chase Dep., p. 177, line 24 - p. 180, line 14.*

502 U.S. 452 (1992); *Aspen Skiing Co. v. Aspen Highlands Skiing Corp.*, 472 U.S. 587 (1985). Microsoft's use of its monopoly power to tie Internet Explorer to Windows and to coerce screen restrictions from OEMs, as well as Microsoft's restrictive agreements with IAPs and ICPs, lack legitimate business justification.

(1) Tying Internet Explorer to Windows 98

Microsoft's enforcement of contractual restrictions that force OEMs to take Internet Explorer lack justification. Some consumers prefer the latest operating system release without Internet Explorer attached, and some OEMs wish to meet the demand. There is no reason related to efficiency for preventing this natural accommodation from occurring.

To the contrary, the only objective Microsoft's contractual restrictions serve is to thwart consumer choice and to impair competition in the browser market. As explained below, customers demand, and OEMs seek to supply, PCs that offer Windows but not Internet Explorer. *See infra*, section IV.B.1(a). It is not difficult for OEMs to remove the software that provides access to the Internet browser functionality that end users regard as the separate browser product from Windows 98.[41] By prohibiting OEMs from doing so, Microsoft makes both OEMs and consumers who prefer Windows without IE worse off.

Just as the evidence in *Aspen Skiing* showed that the defendant "was not motivated by efficiency concerns and . . . was willing to sacrifice short-run benefits . . . in exchange" for "reducing competition . . . over the long run," 472 U.S. at 602-03, so too the evidence here

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[41]In Windows 98, Internet Explorer provides a small number of Internet-oriented updates that are not available through the installation of Internet Explorer, as distributed separately from the operating system, on top of Windows 95 or any other operating system to which IE has been written. Whatever few embedded links to Internet Explorer Microsoft has put in Windows 98, the core reality is that users, for the purposes of understanding their ability to browse, will perceive Windows 98 as effectively little more than the combination of Windows 95 and Internet Explorer 4. *See, e.g., F. Santos Deposition, p. 18, lines* 16-23. Microsoft has not discouraged this perception, and acknowledges that the browsing functionality in Windows 98 is almost entirely equivalent to that provided when Internet Explorer 4.01 is installed on top of Windows 95. *See C. Jones Deposition, p. 34, lines 2-8.* This functionality may readily and without change to the fundamental design of the operating system be either removed or made to respect the user's choice of browser. Contrary to Microsoft's recent ambiguous suggestion before the Court of Appeals that doing so cannot "facilely" be accomplished, *see Microsoft Motion for Stay, 5/5/98,* and were Microsoft less interested in "welding" Internet Explorer to Windows 98, *see Exhibit 74 (MS7 006219), 2/8/97 W. Veghte e-mail to M. Dunie*, it presumably would recognize that removing IE from Windows 98 from the end user's perspective is not difficult.

demonstrates that Microsoft is denying consumers options they prefer. Microsoft's actions are driven by its overriding, strategic objective of maintaining its monopoly by winning the browser war. Its refusal to provide alternatives customers want results from its effort to exclude competitors and preserve its operating system monopoly. *See Sibley Decl.*, ¶¶ *48, 49.*

(2) Microsoft's Screen And Boot-Up Sequence Restrictions Serve No Legitimate Purpose

The usual (and usually unsuccessful) argument of the typical antitrust defendant is that its restrictions are justified by quality control concerns. But the facts will not support such an argument here. Any such claim by Microsoft would be pretextual and therefore cannot save its exclusionary conduct. *See Eastman Kodak,* 504 U.S. at 484-86.

A quality control defense is implausible here for several reasons. Microsoft requires OEMs to bear the costs of providing post-sale support costs for the computers they sell (including the cost of responding to customer problems or inquiries with respect to Windows). *See, e.g., McKinney Dep., p. 18, line 25 - p. 19, line 6; Romano Dep., p. 21, lines 9-20*. Accordingly, OEMs are unlikely to take any action that will do anything that increases the likelihood that customers will call them for technical support. This includes making software modifications that will crash the system, slow its operation, or create a confusing sequence of displays -- the very things Microsoft is likely to claim as the harms its boot-up and screen restrictions seek to prevent. Indeed, after Microsoft enforced the restrictions against one major OEM that had inserted a customized user interface providing a tutorial and a simplified menu of application choices (including Internet software), the OEM discovered that the removal of the interface significantly increased support calls. *See Romano Dep., p. 18, line 23- p.19, line 17*; *Exhibit 99 (HP-MSN 0784-785)*. Even after the OEM brought this to Microsoft's attention, Microsoft refused to relax the restrictions. *Ibid.*

Notably, without quality control objections, Microsoft permits OEM modifications that do not threaten its monopoly. For example, in Windows 98 Microsoft will grant exceptions to the screen restrictions for some OEM tutorials and "system check" applications, even though these

modifications may result in an inconsistent user experience with Windows. *See Kempin 3/98 Dep., p. 58, line 24 - p. 59, line 25*. Similarly, Microsoft will permit substantial modifications *if* the OEM agrees to make such modifications using proprietary Microsoft technology. For instance, Microsoft will permit OEMs to preinstall large, dynamic icons and displays on the Windows desktop, but *only* if (1) the OEM uses the Active Desktop, and (2) limits its conduct to OEM-specific (and not third party) promotions. *See Exhibit 98, The Windows Experience Phase II (MSV 0009404A)* (OEMs will be allowed to add OEM-branding to the boot-up process provided that no third party advertising occurs; Microsoft will only allow third party service providers into the Windows "feature set" if they help Microsoft "strategically"); *Exhibit 76 (MS7 004364), 4/3/97 K. Kolb e-mail*. By contrast, Microsoft prohibits modifications it perceives will foster competitive threats. One recent Microsoft document explains that the addition of utilities such as virus scans and device driver installers are "minor issues" and a "common exception," but that one OEM's design of an icon for the OEMs' Internet referral service offering that is more prominent than Microsoft's Internet Connection Wizard icon is a "serious breach." *See Exhibit 77 (MS7 007108), K. Kolb 12/1/97 e-mail*.

Because Microsoft has enforced the boot-up sequence and screen restrictions principally when it suits its purpose of excluding rivals, any quality control justification advanced by Microsoft should be rejected here.

(3) Microsoft's Exclusionary Contracts With IAPs And ICPs Are Naked Restraints On Competition, Lacking Legitimate Business Justification

Microsoft may contend that its IAP and ICP contracts were merely designed to provide Internet Explorer additional promotional and distributional opportunities. *Myhrvold Dep., p. 75, lines 10-22; Chase Dep., p. 213, lines 1-7, p. 216, lines 5-12*. This explanation, however, does not address the exclusive (or near-exclusive) nature of the contracts. Microsoft could have secured distributional opportunities for Internet Explorer, including a requirement that Internet Explorer be distributed to new subscribers generated through distribution with Windows, without restricting the distribution of third party browsers. *See Sibley Decl., ¶ 41*.

Microsoft's executives have confirmed that Microsoft's agreements are intended to exclude rivals. Cameron Myhrvold, for instance, explained that Microsoft was "concerned" that if

IAPs shipped Internet Explorer "side by side with Navigator," a user might become confused about which browser was "preferred" and select Navigator. *Myhrvold Dep., p. 89, lines 6-20, p. 92, lines 3-21, p. 99, lines 9-25.* Indeed, Mr. Myhrvold credited some of these exclusionary provisions to Microsoft simply "getting aggressive" -- indeed, "overly so" -- and crafting creative ways "to advantage and promote IE." *Id at p. 103, lines 6-7; p. 75, lines 16-17.*

Similarly, any business explanation Microsoft could plausibly claim for the ICP restrictions is inconsistent with limiting the restrictions to only the top two "Other Browsers." In other words, Microsoft's agreements are intended to undercut competitive threats and are not designed simply to aid Microsoft in any legitimate effort to compete on the merits against whomever else (other than rival browser producers) might compete with Microsoft for ICP support.[42] Indeed, in the course of negotiations relating to the restrictions, ICPs understood that the restrictions were specifically aimed at Netscape. *See, e.g., Colburn Dep., p. 49, line 9 - p. 50, line 12; Declaration of Steve Wadsworth ¶ 8.*

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Because Microsoft's exclusionary conduct lacks any legitimate business justification, that conduct violates Section 2 of the Sherman Act. But even if Microsoft advanced some explanation for its conduct, it would still amount to unlawful maintaince of monopoly power. It is settled that a monopolist violates Section 2 if it "maintain[s] monopoly [power] by means of those restraints of trade which are cognizable under [Sherman Act] § 1." *United States v. Griffith*, 334 U.S. 100, 106 (1948); *United States v. United Shoe Mach. Corp.*, 110 F. Supp. 295, 342 (D. Mass. 1953), *aff'd per curiam*, 348 U.S. 521 (1954); *Barry Wright Corp. v. ITT Grinnell Corp.*, 724 F.2d 227, 239 (1st Cir. 1983). As explained below, Microsoft's conduct independently violates Section 1 of the Sherman Act; and because that conduct threatens to contribute to Microsoft's monopoly power these Section 1 violations each independently establish a violation of Sherman Act Section 2.

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[42]For example, non-browser "push" products developed by companies such as PointCast, Yahoo, and Marimba also seek deals with ICPs to aggregate and to carry content to end users. Though Internet Explorer arguably competes with such firms for ICP content, Microsoft apparently has made no attempt to include them within the scope of its restrictive contractual provisions.

b. Microsoft's Contractual Restrictions With OEMs, IAPs, And ICPs Unreasonably Restrain Trade In Violation Of Sherman Act Section 1

Without exception, Microsoft implements the exclusionary conduct challenged in this case through agreements with OEMs, IAPs, and ICPs. Because its restrictive conduct is therefore not "wholly unilateral," *Copperweld Corp. v. Independent Tube Corp.*, 467 U.S. 752, 768 (1984) (internal quotations omitted), it is subject to scrutiny under Section 1 of the Sherman Act, which prohibits "unreasonable restraints of trade". Some of this conduct -- Microsoft's tying of Internet Explorer to Windows -- is illegal *per se* (that is, conclusively unreasonable if proven). Other conduct -- Microsoft's agreements with IAPs and ICPs, and its OEM boot-up sequence and screen restrictions -- require analysis under the "rule of reason," and are illegal under Section 1 because they injure competition without offsetting procompetitive benefits. *See United States v. National Soc'y of Prof. Eng'rs*, 435 U.S. 679, 687-92 (1978); *Chicago Board of Trade v. United States*, 247 U.S. 231, 238 (1918); *Standard Oil Co. v. United States*, 211 U.S. 1, 60-61 (1911).

i. *Microsoft's Tying Of The Internet Explorer Browser To Windows 98 Is A Per Se Violation Of Section One*

"A tying arrangement is 'an agreement by a party to sell one product but only on the condition that the buyer also purchase a different (or tied) product, or at least agrees that he will not purchase that product from another supplier.'" *Eastman Kodak Co. v. Image Tech. Servs., Inc.*, 504 U.S. 451, 461 (1992) (quoting *Northern Pac. R. Co. v. United States*, 356 U.S. 1, 5-6 (1958)). Such arrangements are unlawful *per se* when the seller "exploits its market power" in the tying product market "to force the buyer into the purchase of a tied product that the buyer either did not want at all, or might have preferred to purchase elsewhere on different terms." *Jefferson Parish Hosp. Dist. No. 2 v. Hyde*, 466 U.S. 2, 12-14 (1984). Accordingly, to establish *per se* illegality, the United States need demonstrate (1) the existence of two separate products; (2) the sale of one product (the tying product) conditioned on the purchase of the other product (the tied product); (3) the seller's possession of sufficient market power to compel acceptance of the tied product; and (4) the foreclosure of a not insubstantial amount of commerce in the tied product market. *See Eastman Kodak*, 504 U.S. at 462; *see also Foster v. Maryland State Savs. & Loan Ass'n.*, 590 F.2d 928, 931 (D.C. Cir. 1978).

(1) Windows 98 And Internet Explorer Are Separate Products For Tying Law Purposes

Whether a package consists of one or more separate products depends not on the functional relationship between the components, but rather on the "character of demand" for them. *Jefferson Parish,* 466 U.S. at 19. Two products exist for tying law purposes if "there [is] sufficient consumer demand so that it is efficient for a firm to provide" them separately. *Eastman Kodak,* 504 U.S. at 462 (internal quotations omitted). As explained below, Microsoft's forced licensing of Internet Explorer with Windows 98 impermissibly links together "two separate product markets." *Jefferson Parish,* 466 U.S. at 21.

(a) Microsoft's Distribution Practices Demonstrate The Existence Of Separate Demand For Internet Browsers

There is plainly substantial consumer demand for browsers independent of operating systems. In fact, even though Microsoft's forced licensing of Internet Explorer (among other things) has made the OEM channel a significant one for browser distribution, most computer users have obtained their Internet browser separately, and at different times, from the Windows operating system.

Microsoft recognizes the separate demand for the two products by engaging in a wide variety of marketing conduct directed specifically at its browser. It has given its browser a separate name and regularly calls it a "product," not a component of or update to Windows.[43]

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[43]For example, its standard End User License Agreement for Internet Explorer 3.0, which comes in the retail box Microsoft advertises as containing Internet Explorer, labels IE as a "product," rather than an update to the operating system, and makes no mention of Windows. *See Exhibit 78, Microsoft Internet Explorer Retail End User License Agreement.* Similarly, upon downloading Internet Explorer 4.0, the user is presented with a license that defines the browser as a "software product" to be used "in conjunction with" Windows 95. *See Exhibit 79, Internet Explorer Download End User License Agreement*. The license does not say "as part of" Windows 95, or contain any language to that effect.

Microsoft was deliberate in naming the Internet Explorer a browser and in promoting it as a product separate from Windows. This decision stemmed from the character of the market's demand. For example, a Microsoft marketing executive testified:

Q: Do you ever tell ISPs that they are distributing a component of Windows?

A: . . . No, I don't think we tell them that. Obviously, they understand our plans and intentions and are supportive of that. But no it's not something I go out and specifically flag.

Q: Why not?

A: Well, if you're selling tires, you probably don't want to sell them as piece of a Ford.

Q: Why not?

Indeed, Microsoft *never* represented to its customers that Internet Explorer is an update to or component of its operating system rather than a separate product until the United States brought an action to enforce the terms of the 1995 Final Judgment.[44] To the contrary, it has engaged in a concerted, massive advertising campaign for Internet Explorer; entered into numerous marketing relationships with OEMs, ISPs, and content providers specifically to promote Internet Explorer 4.0;[45] separately tracked the market penetration and usage of Windows and Internet Explorer in what it sees and often describes as two separate markets, comparing them to a wholly different set of competitors;[46] distributed IE as a product distinct from Windows through a variety of channels, including distribution through ISPs and OLS, bundled with other hardware and software products, at retail in packages Microsoft labels as the Internet Explorer Plus (IE 4.0) and the Internet Explorer Starter Kit (IE 3.02), and even in the OEM channel, in which it has licensed Internet Explorer separately from Windows for distribution on product support CDS.[47]

A: I don't think that's what people are buying.
Myhrvold Dep., p. 26, line 21 - p. 27, line 9.

[44]Indeed, it appears that Microsoft has undertaken, after its experience in litigation on this issue, to "correct" the presentation of Internet Explorer. *See supra,* fn. 3.

[45]*See, e.g., Exhibit 7, Memorandum of Understanding re Intenret Explorer 4.0 with Gateway, Packard Bell/NEC Corp., Hwelett-Packard Co., Toshiba Ameircan Information Systems, Inc. (MSV 10001-10038) (detailing aspects of program to promote the"IE 4 browser" but not mentioning "Windows").*

[46]*See, e.g., Maritz Dep., p. 29, line 3 - p. 30, line 6 (Microsoft interested in having its share of browser market exceed Netscape's share); Silverberg Dep., p. 19, line 6 - p. 20, line 9 (after release of Windows 95, Microsoft has tracked IE share primarily against Netscape Navigator, because Navigator is "a competitive platform technology to Windows"); Jones Dep., p. 92, lines 10-25 (Microsoft tracks IE share primarily against Netscape); Exhibit 80 (MS7 004624), D. Cole 8/6/97 e-mail ("Number 1 goal for IE continues to be market share. Let's not forget that. We should be aggressive here to force ourselves to think about breakthrough ways to gain share. We should be after 50% by the end of FY98 (June 98), and 75% by the end of FY99 which is June 99."); Exhibit 81 (MS6 6009915-18), (tracking IE share in comparison to NN and separately from the installed base of Windows operating systems); Exhibit 82 (MS6 6013328-32), Yusuf Mehdi 11/4/96 IE 3.0 Sustain Marketing Plan e-mail (tracking browser share against Netscape).*

[47]*See, e.g.. Exhibit 9 (MSV 0005734- 5747), License and Distribution Agreement (Microsoft Internet Explorer) between Compaq Computer Corp. and Microsoft (agreement to promote Internet Explorer that makes no reference to Windows).*

Moreover, even after the release of Windows 98 Microsoft will continue to release new versions of Internet Explorer, thus recognizing that there will be continuing demand for browser products apart from operating system purchases. Indeed, Microsoft has publicly stated that it will release Internet Explorer 5.0 later this year, enabling end users to update the browser without switching to Windows 98.[48]

However, the most clear and unambiguous indication of Microsoft's recognition of demand for browsers separate from operating systems is the fact that Microsoft has made each version of Internet Explorer available for *non-Microsoft* operating systems and plans to continue doing so after the release of Windows 98. Internet Explorer 3.0 has been ported to Apple Computer's Macintosh operating systems (as well as Microsoft's Windows 3.1 operating system, with which Internet Explorer is not bundled); Internet Explorer 4.0 is now available for Windows 3.1, the Macintosh, and Sun Microsystems' Solaris (a version of Unix) operating systems and will soon be available for other versions of Unix, including HP-UX, IBM AIX, and SGI IRIX; and Microsoft will make Internet Explorer 5.0 available for users of Windows 3.1, Macintosh, and Unix. *See, e.g., Chase Dep., p. 98, line 12 - p. 99, line 1; Jones Dep., p. 115, line 10 - p. 116, line 14.*

The non-Windows versions of Internet Explorer, in addition to sharing a name with the Windows 95 version, look and feel essentially the same as that version to end users.[49] *See, e.g., Myhrvold Dep., p. 37, line 25 - p. 38, line 25.* Indeed, one of Microsoft's primary motivations for developing non-Windows versions of Internet Explorer has been its recognition of the need to meet specific customer demand for such versions, wholly apart from Windows. *See Chase Dep.,*

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[48]*See, e.g., Chase Dep., p. 94, lines 7-22; Jones Dep., p. 114, line 11 - p. 115, line 4.*

[49]Because different specific software code is needed to interact with different operating systems, the actual code underlying the Internet browser functionality is somewhat different for the IE versions that run on different operating systems. However, the demand that Internet Explorer satisfies (as separately available) when used with other operating systems is the same demand for a Internet browser that Internet Explorer satifies when used with Windows. This is confirmed by Microsoft's own marketplace behavior. Microsoft perceives the distribution of a cross-platform browser to be crucial in gaining browser share, which it calculates without regard to technical differences between the different versions of IE. *See, e.g., Exhibit 65 (MS6 6003202), Internet Client and Collaboration 3 Year Business Outlook, 2/11/97 (listing a late release of IE 4 for other platforms as a "risk"); Exhibit 85 (MS6 5005667-92), P. Maritz e-mail on winning the browser battle (developing a cross platform browser as a strategy).*

p. 99, lines 2-18; Myhrvold Dep., p. 35, line 20 - p. 39, line 9. And in tracking Internet Explorer market share, Microsoft aggregates across platforms, including those versions of Internet Explorer for other operating systems in its calculus. *See Exhibit 54 (MSV 10545).* Indeed, Microsoft's efforts to separately port versions of Internet Explorer for other operating systems, and to distribute those versions to ISPs and ISVs (as well as directly through other operating system vendors), demonstrate that there is "sufficient consumer demand so that it is efficient" for Microsoft to provide its browser products separately from its operating system products.[50] *Eastman Kodak*, 504 U.S. at 462.

(b) Microsoft's And OEMs' Marketplace Behavior Demonstrates The Existence Of Separate Demand For Windows

There is also substantial consumer demand for Windows (and, more generally, for operating systems) apart from Internet browsers. Indeed, Microsoft specifically recognized this demand and took steps to meet it. David Cole, a Vice President of Microsoft in charge of the development of Internet Explorer, conceded in proceedings before the Court that Microsoft chose to disseminate instructions for "uninstalling" Internet Explorer through the Add/Remove Programs utility in Windows 95 precisely because of demand from corporate customers who want Windows but not Internet Explorer. *January 14, 1998 A.M. Hearing Transcript, pp. 4, 48-50; D. Cole Dep., p. 50, line 2 - p. 51, line 24.*[51]

Microsoft is not alone in recognizing and seeking to satisfy demand for Windows without a browser. OEMs recognize that their customers sometimes want to purchase PCs with an operating system but no browser, *see Declaration of Richard Dean Williams, 4/29/98, ¶ 6;*

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[50] Interestingly, Microsoft executives have explicitly considered suggestions to substantially curtail or even abandon cross-platform Internet Explorer development. *See, e.g., Exhibit 86 (MS7 007422), J. Allchin 2/18/97 e-mail to B. Gates and P. Maritz.* By *not* following advice to deemphasize cross-platform development of IE, Microsoft has bowed to the power of separate demand for browsers and operating systems.

[51] Also in response to customer demand for Windows 95 without a Internet browser, Microsoft published a method for removing IE 4.0 from Windows 95 in the Microsoft "Knowledge Base," a collection of technical articles Microsoft makes available to the public through, among other means, the Microsoft website. *Exhibit 88, Removing Internet Explorer 4.0 for Windows 95 Using Ieremove.exe, Q166313, Oct. 17, 1997.*

Ransom 3/19/98 Dep., p. 9, line 11 - p. 10, line 4, a fact Microsoft executives acknowledge, *see Chase Dep. p. 80, lines 10-17, Exhibit 17 (MSV 09129A), C. Jones (1/15/96) e-mail (*"Some [OEMs] want to remove the icon from the desktop -- our response should be that it is not allowed"). Indeed, one major OEM expressly requested that Microsoft amend its Windows 95 license agreement to permit it not to ship Internet Explorer preinstalled with Windows 95. One of its executives explained this request as follows:

> Some business and government customers prefer not to have Internet Explorer preinstalled on their computers because: (1) the customer may have its own software or software standards which do not include the latest version of Internet Explorer; (2) the customer may wish to install a competitive browser instead of Internet Explorer; or (3) the customer may wish to prevent its employees from accessing or attempting to access the Internet or World Wide Web.

Declaration of Joseph J. Kanicki, 4/29/98, ¶ 2. Unlike its course of action with respect to any other major OEM, *see infra*, section IV.B.1(b), Microsoft granted this OEM's request, requiring it to ship Internet Explorer with its Windows 95 PCs "[u]nless specifically requested to the contrary by the end user . . . ." *See Exhibit 89 (MSV 0000749-65), Amendment 2 to License Agreement for Operating Systems, 5/2/96.* Notably, since the request was granted, a number of customers have in fact either requested the removal of Internet Explorer or provided master "images" of the software, not including IE, they wish installed on numerous PCs to be purchased by the customer. *See Exhibit 90, Response of Dell Computer Corporation to U.S. Department of Justice CID 18016, April 14, 1998, p. 1.*[52]

Demand for Windows without a preinstalled browser, moreover, extends beyond the preferences of corporate customers. As discussed above, some OEMs wish to offer their customers only a single browser -- selected by the OEM rather than by Microsoft -- to avoid potential desktop "clutter"; to avoid customer confusion caused by having multiple browsers preinstalled and visible on the desktop; to avoid increased technical support costs resulting from offering two browsers; or to minimize product testing costs. *See supra*, section IV.A.3(b).

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[52]As discussed below, absent the amendment, the OEM would not be permitted to preinstall the image with IE removed. *See infra*, section IV.B.1(b).

Based on various combinations of these considerations, over the past three years several of the largest OEMs in the United States have deleted or requested the ability to delete at least the Internet Explorer icon from the Windows desktop. *See, e.g., Romano Dep., p. 33, line 14 - p. 43, line 19; Browning Decl. ¶8; Exhibit 18, Gateway 2000, Inc. 9/19/97 Answers to Interrogatories, p. 8; Decker Dep., p. 18, line 21 - p. 21, line 6.*[53] Moreover, since the United States and Microsoft entered into the January 22, 1998 Stipulation, which provided OEMs the freedom to remove Internet Explorer from Windows, several OEMs have taken steps to invoke this freedom. *See Kies Dep., p. 10, line 12 - p. 11, line 22*; *Brownrigg 3/98 Dep., p. 30, line 7 - p. 31, line 20.*

As noted above, Microsoft responded to consumer demand for Windows 95 without a browser by disseminating instructions for "uninstalling" Internet Explorer using Windows' Add/Remove program utility.[54] Microsoft does *not* intend to provide a comparable option for removing Internet Explorer from Windows 98, although OEM witnesses have testified that demand for Windows without a Internet browser persists. As one OEM executive explained:

> Our corporate customers we have had most success with in our marketing are very specific about what software applications that they ship, or excuse me, that their end users use on their notebook computers. They do not like to have choices forced upon them, but would rather choose themselves which ones they use. So in accordance with this we are providing them with the most choices that we can provide by not including a browser and letting them select whichever browser best fits their needs. *Kies Dep., p. 11, lines 13-22.*[55]

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[53]As discussed below, *see infra*, section IV.B.1(b), Microsoft has with only a single exception refused these OEM requests and has even threatened to revoke OEMs' Windows 95 licenses after the OEMs deleted the Internet Explorer and MSN icons.

[54]The mechanism for removing IE embodied in the 1/22/98 stipulation is the Windows 95 Add/Remove Programs utility. As noted above, Microsoft designed IE to be removable using this feature specifically in response to end-user demand for a browserless user interface.

[55]Another executive with the same OEM, in a Declaration provided *at the request of Microsoft*, reiterates this point:

> [I]n response to requests from certain corporate customers for personal computers containing a bare minimum of preinstalled software, we opted to place as much value-added software as possible on a separate CD-ROM, delivered with the machine, to simplify the configuration process.

This is, of course, *exactly* the freedom of choice sought by the United States in this case.

OEMs' interest in the option of shipping Windows 98 PCs without IE preinstalled, *see, e.g., Kies Dep. at p. 15, lines 6-18*, is particularly understandable given the fact (as well as OEMs' perception) that Windows 98 updates Windows 95 in a variety of ways unrelated to the browser (*e.g.*, support for an expanded array of hardware devices), and that customers (including customers who do not want Internet Explorer preinstalled) will likely demand these new features. *See id., p. 15, line 6 - p. 17, line 11; Kempin 3/98 Dep., p. 20, lines 8-17, p. 21, line 14 - p. 23, line 12; Veghte Dep., p. 36, line 25 - p. 37, line 15.*

Not surprisingly, at least one major OEM has already explored the possibility of eliminating Internet Explorer from the Windows 98 desktop in connection with providing customers a choice of browsers, and has inquired whether it may have the freedom to eliminate at least (and perhaps more than) the Internet icon off the desktop for customers that prefer a different browser.[56] *See Brownrigg 3/98 Dep., p. 30, line 7 - p. 31, line 20; Von Holle 4/30/98 Dep., p. 15, line 25 - p. 17, line 23*. An executive with another OEM has expressed interest in being able to provide such customers Windows 98 without Internet Explorer. *Kies Dep., p. 15, line 6 - p. 17, line 11*. Yet another has stated that it would at least "consider offering its customers the option" of obtaining "a version of Windows 98 without IE 4," should one be made available. *Williams Decl., ¶ 14.* In sum, OEMs plainly desire the freedom to meet their customers' demand for the latest version of Windows without being compelled to thwart their

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> It was in that context that we opted to remove the Internet Explorer icons from the Windows desktop and the Start menu. . . .

Declaration of Craig Rittenhouse, 4/30/98, ¶ 4. This executive points out that including Internet Explorer on a separate CD-ROM will enable end users to "upgrade the operating system to that level of functionality if they *choose* to do so." *Id. at ¶ 6 [emphasis added]*. The OEM also plans to include a non-Microsoft browser on the same CD-ROM, so that users can choose the browser they wish to have, thereby "upgrading the operating system" with the browser product of their choosing. *See Kies Dep., p. 11, lines 1-6.* Mr. Rittenhouse's use of the term "upgrade the operating system" with respect to a user's installation of a browser makes plain that "upgrading the operating system" is a fair characterization of what *any* application product does when installed by an end user or an OEM. The words used to express this result have no bearing on whether the application is a separate product from the operating system.

[56] As discussed above (*see supra*, section IV.B.1(a)(2)), Microsoft has denied the request, as it has generally denied similar requests with regard to Windows 95.

customer's preference to include the browser of their choice or no browser at all.

(c) The Combination Of Windows And Internet Explorer, Bundled Together As Windows 98, Does Not Constitute A New, Single Product For Tying Law Purposes

Microsoft may assert that the combination of Windows and Internet Explorer in Windows 98 represents a single "new product." But the issue is not whether Microsoft can design Windows 98 as it has. When a tie is enforced through coercive contractual restraints, two products do not become one just because they are "functionally linked" or "functionally integrated." *Jefferson Parish*, 466 U.S. at 19 ("the answer to the question whether one or two products are involved turns not on the functional relation between them, but rather on the character of demand for the two items"); *Eastman Kodak*, 504 U.S. at 462 ("We have often found arrangements involving functionally linked products at least one of which is useless without the other to be prohibited tying devices." (Internal quotation omitted)). Indeed, the Supreme Court has "often found arrangements involving functionally linked products at least one of which is useless without the other to be prohibited tying devices." *Jefferson Parish*, 466 U.S. at 19, n. 30 (citations omitted). Similarly, the bundling of two products should not be considered a single product simply because the combination represents an "effort to improve the [tying product] by adding elements to it." *Multistate Legal Studies, Inc. v. Harcourt Brace Jovanovich Legal & Prof. Pub., Inc.*, 63 F.3d 1540, 1547 (10th Cir. 1995).

Here, Microsoft did not just design Windows 98, but rather -- and this is the crucial point about the tie-in -- has used its market power in Windows to contractually prohibit OEMs from unbundling Windows 98 and the Internet Explorer browser. That kind of contractual restraint goes to the heart of what Section 1 prohibits. This case consequently does not raise the concerns that have caused Courts to treat more leniently challenges to product designs brought under Sherman Act Section 2

(2) Microsoft Uses, And Will Use With Regard To Windows 98, Its Power To Coerce OEM Acceptance And Distribution Of Internet Explorer

For a tying arrangement to exist, the purchase (or licensing) of the tying product must be "conditioned" on the acceptance of the tied product. *Eastman Kodak*, 504 U.S. at 461-62. The

pertinent inquiry is whether licensees "might have preferred" not to license the tied product, or to license it "elsewhere on different terms," *Jefferson Parish*, 466 U.S. at 12, and whether the licensor "coerces the abdication of [licensees'] independent judgment" as to the relative merits of competing products in the tied product market. *Times-Picayune Publishing Co. v. United States*, 345 U.S. 594, 605 (1953).

The requisite coercion clearly exists in this case. Microsoft intends to offer Windows 98 as a single package including Internet Explorer. *See supra*, section IV.A.3(a). Even more significantly, Microsoft (1) has imposed (with respect to Windows 95) and plans to reimpose (with respect to Windows 98) licensing restrictions prohibiting OEMs from deleting Internet Explorer; (2) has consistently and adamantly applied these restrictions to deny OEM requests to remove Internet Explorer; and (3) has conditioned Windows licenses on OEM acceptance of Windows by threatening OEMs that have in fact removed means of access to Internet Explorer (such that an ordinary end user could not use the program, even if underlying program code remained on the PC) with termination of their Windows licenses unless they restored the ability to access IE. Thus, OEMs that have *actually* preferred to license Windows 95, and have expressed a desire to license Windows 98 with Internet Explorer removed, have been forced to abandon that preference.

In the case of at least two major OEMs that removed Internet Explorer from the Windows desktop, Microsoft has explicitly conditioned the continued licensing of Windows 95 (invoking the licensing restrictions described above) on the OEMs' restoring IE. *See, e.g., Romano Dep., p. 34, line 4 - p. 42, line 11; Decker Dep., p. 18, line 21 - p. 19, line 3*. Recognizing the dependence of their PC business on continued access to Windows 95, both OEMs quickly complied, thereby retaining their Windows 95 licenses. *See Romano Dep., p. 42, lines 7-11; Decker Dep., p. 20, line 21 - p. 21, line 14*. Still other OEMs, rather than suffering Microsoft's wrath by actually removing Internet Explorer, asked Microsoft for permission and were refused. *See Browning Declaration, ¶¶ 7-8; Exhibit 18, Gateway 2000, Inc. 9/19/97 Answers to Interrogatories, p. 8*. Moreover, Microsoft is carrying this policy forward to Windows 98. Already, one OEM has requested permission to delete the Internet Explorer icon, and Microsoft has denied the request. *See Von Holle 4/98 Dep., p. 15, line 25 - p. 17, line 19.*

As a direct result of Microsoft's enforcement of contractual restrictions to prohibit the removal of Internet Explorer from Windows 95, OEMs have abandoned their efforts to preinstall Windows without Internet Explorer. *See, e.g., Decker Dep., p. 21, lines 7-14; Browning Decl., ¶¶ 7-8; Von Holle 4/98 Dep., p. 18, line 14 - p. 19, line 14.* But for Microsoft's efforts to enforce the tie of Internet Explorer and Windows through the exercise of its contractual rights, some OEMs would not have licensed and preinstalled Internet Explorer. Still other OEMs undoubtedly would have engaged in a more detailed assessment of the merits of competing browsers had Microsoft not enforced its license agreements to prevent Internet Explorer's removal. *See, e.g., Ransom 3/98 Dep., p. 29, lines 8-19.*

(3) Microsoft Possesses Power In The Tying Product Market

Tying law's *per se* rule requires that the defendant possess only market -- not monopoly -- power in the tying product market. *See, e.g., Eastman Kodak*, 504 U.S. at 464. As discussed above, of course, Microsoft possesses *monopoly* power in the personal computer operating system market. Accordingly, the United States plainly has demonstrated that Microsoft possesses the power "'to force a purchaser to do something that he would not do in a competitive market.'" *Eastman Kodak*, 504 U.S. at 464 (quoting *Jefferson Parish*, 466 U.S. at 14).

(4) The Tie Affects A Not Insubstantial Volume Of Commerce in Both The Tied And Tying Markets

In order for a tie to be unreasonable *per se*, it must foreclose a not insubstantial volume of commerce. *See Jefferson Parish*, 466 U.S. at 16; *International Salt Co. v. United States*, 332 U.S. 392, 396 (1947). Microsoft's forced licensing of Internet Explorer affects virtually the entire market through which new computers are sold. This unquestionably establishes the requisite potential for foreclosure in the tied product market that triggers tying law's *per se* rule. *See, e.g., United States v. Loew's Inc.*, 371 U.S. 38, 49 (1962) (as little as $60,800 in affected sales suffices); *Fortner Enterprises Inc. v. United States Steel Corp.*, 394 U.S. 495, 501 (1969) ($190,000 foreclosed not an insubstantial amount, even though a very small percentage of the market).

Moreover, the effects of Microsoft's forced licensing of Internet Explorer extend far beyond that necessary to establish *per se* illegality. The tying of Internet Explorer threatens to

foreclose competing Internet browers; and this foreclosure, in turn, threatens to eliminate what Microsoft perceives as a significant challenge to its operating system monopoly. *See supra*, section IV.A.3(b). This implicates the central concern of tying law: that a monopolist, by "'exploiting his dominant position in one market to expand his empire into the next,'" *Eastman Kodak*, 504 U.S. at 479 n.29 (quoting *Times-Picayune*, 345 U.S. at 611), may erect barriers to entry that reinforce its monopoly power. *See Grappone, 858 F.2d at 759. See generally 10 P. Areeda, et al., Antitrust Law* ¶¶ 1747a-c, at 230-33 (1996) (explaining that the tying "of partial substitutes [is] more dangerous than the typical tie" because it may foreclose those producers who possess "the skill to be potential entrants in the tying product market").

(5) Microsoft's Tying Arrangement is Per Se Illegal

Microsoft's conditioning of a license to Windows 98 on an OEM's licensing Internet Explorer consequently is unlawful *per se*. Even if it were appropriate to entertain a defense to *per se* illegality when the anticompetitive effects of a tying arrangement are outweighed by procompetitive effects, *cf. Mozart Co. v. Mercedez-Benz of N. Am., Inc.*, 833 F.2d 1342, 1348-51 (9th Cir. 1988), such a defense could not succeed here. Microsoft, as explained above, cannot demonstrate any procompetitive reason for enforcing its licensing agreements to prevent OEMs from removing Internet Explorer -- let alone substantiate a justification that would outweigh the harm to competition caused by threatening to eliminate the most significant competitive threat to Windows' dominance. *See supra* IV.A.5.

ii. *Microsoft's Boot-Up Sequence And Screen Restrictions, And Agreements With IAPs And ICPs, Unreasonably Restrain Trade*

Microsoft's boot-up sequence and screen restrictions reduce competition between Internet Explorer and competing Internet browsers and prevent OEMs from differentiating their products to meet consumer demand. The restrictions also are among the means by which Microsoft's anticompetitive contracts with IAPs and ICPs are extracted and its tying of Internet Explorer and Windows is enforced. As noted above, Microsoft's likely justifications for the restrictions are pretextual; but even if valid, they can be served through significantly less restrictive alternatives. *See Sullivan v. NFL*, 34 F.3d 1091, 1003 (1st Cir. 1994) ("One basic tenet of the rule of reason is that a given restriction is not reasonable, that is, its benefits cannot outweigh its harm to

competition, if a reasonable alternative to the policy exists that would provide the same benefits as the current restraint."), *cert. denied*, 513 U.S. 1190 (1995). Accordingly, Microsoft's restrictions violate Section 1.

Microsoft's exclusionary agreements with IAPs and ICPs, among other things, place substantial limits on those firms' ability to distribute and promote competing browsers. *See supra,* IV.A.3(e). When combined with Microsoft's other conduct, the effect of these contracts is to foreclose the most important channels through which non-Microsoft Internet browsers reach customers and to leave competing Internet browers with inadequate means of reaching customers. These agreements are essentially equivalent to exclusive dealing arrangements, which are unlawful when the degree of foreclosure threatens to impair competition. *See Standard Oil Co. v. United States,* 337 U.S. 293 (1949); *Tampa Electric Co v. Nashville Coal Co.*, 365 U.S. 320 (1961). And because Microsoft's exclusionary agreements significantly impair competing browsers' access to the most significant channels by which consumers acquire browsers, and lack any procompetitive justification, they are unlawful. *See, e.g., United States v. Dairymen, Inc.*, 1985-1 Trade Cas. (CCH) ¶ 66,638, at 66,156-57 (6th Cir. 1985) (*per curiam*) (invalidating exclusive dealing arrangement covering 50% of the market's volume).

Here, the degree of foreclosure takes on added significance because Microsoft's exclusionary contracts threaten to "tip" the browser market decisively in Microsoft's favor. *See Sibley Decl. ¶ 51*. The possibility that the browser market might tip means that Microsoft's conduct, even if it does not wholly foreclose every distribution alternative for rival browsers, nevertheless may result in a second Microsoft monopoly in the browser market. *See id.* The risk that Microsoft's conduct might cause the browser market to tip provides an added basis for finding that its exclusionary agreements amount to an unreasonable restraint of trade. *See Tampa Elec.*, 365 U.S. at 329 (significance of foreclosure depends on context).

c. Microsoft's Conduct Constitutes Attempted Monopolization Of The Browser Market

In addition to maintaining its operating system monopoly, Microsoft's unlawful conduct constitutes attempted monopolization of the browser market in violation of Section 2 of the Sherman Act. In order to prove attempted monopolization, the United States must prove "(1)

that the defendant has engaged in predatory or anticompetitive behavior with (2) a specific intent to monopolize and (3) a dangerous probability of achieving monopoly power." *Spectrum Sports, Inc., v. McQuillan*, 506 U.S. 447, 456 (1993); *see also Association for Intercollegiate Athletics for Women v. NCAA*, 735 F.2d 577, 585 (D.C. Cir. 1984).

i. *Internet Browsers Constitute A Separate Market For Antitrust Purposes*

As an initial matter, Internet browsers are in a distinct product market. *See Sibley Decl.* ¶ *9*. Other software programs are not reasonable substitutes for Internet browsers. Accordingly, in response to a small but significant and nontransitory increase in the price of browsers, browser users would not switch to some other product to such an extent that this price increase would not be profit maximizing for a hypothetical browser monopolist. *See* U.S. Department of Justice and Federal Trade Commission, Horizontal Merger Guidelines § 1.11 (1992). AOL, for example, considered only Internet Explorer and Navigator for its client side needs. *Colburn Dep., p. 15, lines 5-12, p. 21, line 19 - p. 22, line 4.*

ii. *Microsoft Is Using Its Operating System Monopoly And Engaging In Other Anticompetitive Conduct To Monopolize The Browser Market*

As described above, Microsoft has engaged in various anticompetitive and predatory acts designed to exclude rival Internet browsers. Microsoft has used its Windows monopoly to coerce OEMs to license its Internet browser. *See supra*, sections IV.A.3(a-b). In addition, Microsoft has entered into exclusionary agreements with IAPs, ISVs, and ICPs. *See supra*, sections IV.A.3(c-d). Microsoft thus has impermissibly "employed its market position as a lever to . . . attempt to create . . . a monopoly in another market." *Berkey Photo, Inc. v. Eastman Kodak Co.*, 603 F.2d 263, 275 (2d Cir. 1979). "If monopoly power can be used to beget monopoly, the Act becomes a feeble instrument indeed." *United States v. Griffith*, 334 U.S. 100, 108 (1948).

iii. *Microsoft Possesses Specific Intent To Monopolize The Browser Market*

As the Supreme Court has explained, predatory and unfair tactics may be sufficient in themselves to prove the necessary intent to monopolize. *Spectrum Sports*, 506 U.S. at 459. Here, Microsoft's specific intent to monopolize the Internet browser market may be inferred from the numerous anticompetitive and predatory acts that threaten to achieve that objective.

In addition, Microsoft's specific intent to monpolize the Internet browser market can be

inferred from its attempt to solicit its major competitor, Netscape, to participate in an illegal market allocation scheme. In June 1995, Microsoft executives met with executives of Netscape and made a startling proposal, as described by Netscape Executive Vice-President Marc Andreessen:

> There would be a line drawn metaphorically between that which was in the operating system and that which would not be. They were attempting to establish with us whether we were interested in a relationship whereby we would mutually agree to essentially not compete with each other across that line. They would stay below the line. We would stay above the line.

Deposition of Marc Andreessen at p. 38, lines 7-23. Microsoft went on to tell Netscape that Microsoft intended "to completely own the space defined by people browsing the Internet and doing the other things that our products do on top of the Windows 95 operating system and shell," and offered Netscape a deal: if Netscape stayed away from the Windows 95 browsing market Microsoft would cede to Netscape the non-Windows 95 browser space and allow preferential access to certain Microsoft APIs. *Id., p. 47, line 7 - p.49, line 3.* Microsoft executives emphasized that they could not accept Netscape competing as a platform with its own APIs. *Id., p. 51, line 2 - p. 52, line 3. See also Jones Dep., p. 200, lines 9-18* .

Chris Jones, Microsoft's then Group Program Manager for Internet Explorer who participated in the meeting, recently confirmed that Microsoft intended to persuade Netscape to stay on the solutions side of the line between operating systems and applications. He also admitted that Microsoft "absolutely" intended to persuade Netscape not to compete and offered the prospect of Microsoft staying out of browsers for non-Windows platforms. *See Jones Deposition, pp. 208, line 5 - p. 209, line 6; p. 211, line 22 - p. 212, line 6.*

Although Netscape refused to participate in this illegal scheme, Microsoft's effort to secure such an agreement demonstrates its intent to monopolize the browser market. *Cf. United States v. American Airlines, Inc*., 743 F.2d 1114, 1121 (5th Cir. 1984) (a solicitation to form a cartel in a concentrated market, even if the solicitation is rejected, can in itself constitute an attempt to monopolize), *cert. dismissed*, 474 U.S. 1001 (1985).

Of course, Microsoft did not stop with this unsuccessful attempt, but embarked on the predatory course of conduct described above and in doing so made clear its intent to monopolize

the browser market. Bill Gates sent this message to both actual and potential competitors:

> Our business model works even if all Internet software is free. . . . We are still selling operating systems. What does Netscape's business model look like (if that happens)? Not very good. *Exhibit 5, Financial Times, 6/10/96.*.

Indeed, there is little question that, because of the browser's central role in the cross-platform threat, controlling the browser market was Microsoft's preeminent goal. After Microsoft Group Vice-President Paul Maritz had rejected a proposal intended to increase revenue for Windows 98 by charging separately for the shell portion of Internet Explorer, he explained: "There is talk about how to get more $ from the 1000+ people we have working on browser related stuff, but I have not lost sight of the fact that Browser Share is still an overwhelming objective." *Exhibit 91 (MS7 006970), P. Maritz 7/11/97 e-mail to Yusuf Mehdi.*

Earlier, Maritz had set forth why "job #1 is browser share": "We have to stop the Nav-Web site reinforcement cycle with IE3 and shift it in the direction of Active X. . . . No matter what happens, we have to slow Netscape's ability to drive new protocols/stds down." Mr. Maritz went on to explain that it was "necessary to fundamentally blunt JAVA/AWT momentum and to reestablish ActiveX and non-Java approaches . . . [to] <u>protect our core asset Windows</u> - the thing we get paid $'s for." *Exhibit 92 (MS6 6010346-49), 6/20/96 P. Maritz e-mail (emphasis in original).* In short, Microsoft feared and sought to impede the development of network effects that cross-platform technology like Netscape Navigator and Java might enjoy and use to challenge Microsoft's monopoly. Another internal Microsoft document indicates that the plan was not simply to blunt Java/browser cross-platform momentum, but to destroy the cross-platform threat entirely, with the "Strategic Objective" described as to "Kill cross-platform Java by grow[ing] the polluted Java market."[57] *Exhibit 101 (MS7 033448).*

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[57] As used in Microsoft documents, the term "polluted" appears to refer to Java implementations that only work with Windows. *See, e.g., Exhibit 100 (MSS 0083345), (requesting list of Java developers, so Microsoft can "start polluting them with Windows specific stuff").* Other documents confirm the same point: "Screw Sun, cross-platform will never work. Let's move on and steal the Java language. That said, have we ever taken a look at how long it would take Microsoft to build a cross-platform Java that did work? Naturally, we would never do it, but it would give us some idea of how much time we have to work with in killing Sun's Java." *Exhibit 97 (MS7 026935), P. Sridharan 9/17/97 e-mail.*

Microsoft documents relating to the bundling of Internet Explorer with Windows 98 tell the same story: Microsoft tied the products together to foreclose competition. For example, Microsoft executive Jonathan Roberts directed his subordinates to "to really look at why people who get IE with a new machine switch to Navigator and what is being addressed in IE4.0 to make that difficult." *Exhibit 37 (MS7 006062), J. Roberts 3/28/97 e-mail*. Microsoft's executive Christian Wildfeuer wrote in an internal e-mail:

> It seems clear that it will be very hard to increase browser market share on the merits of IE 4 alone. It will be more important to leverage the OS asset to make people use IE instead of Navigator.

Exhibit 23 (MS7 004343). This was further made clear in a January 5, 1997, presentation to Bill Gates emphasizing: "Integrate with Windows" is the way to "Increase IE share." *Exhibit 3, (MS7 00529-44); see also Exhibit 94 (MS6 6012951-56)* ("If we continue to have minimal share in browsers a lot of our other efforts will be futile.").

Finally, in an internal e-mail entitled "concerns for our future" to his boss, Group Vice President Paul Maritz, Jim Allchin, explained the reasons for tying Internet Explorer to Windows:

> 1. **Ensuring that we leverage Windows**. I don't understand how IE is going to win. The current path is simply to copy everything that Netscape does packaging and product wise. . . . My conclusion is that we must leverage Windows more. Treating IE as just an add-on to Windows which is cross-platform [is] losing our biggest advantage -- Windows marketshare. We should dedicate a cross group team to come up with ways to leverage Windows technically more . . . We should think first about an integrated solution -- that is our strength. *Exhibit 94 (MS6 6012884), Megan Bliss and Rob Bennett 12/20/96 e-mail.*

Just two weeks later, on January 2, 1997, Allchin reiterated the same theme in another e-mail to Maritz, this time making explicit that his references to "leveraging" Windows concerned marketing and distribution advantages at least as much as any technical attributes Microsoft believes might be achieved through the "integration" of Internet Explorer:

> "You see browser share as job 1. . . . . I do not feel we are going to win on our current path. We are not leveraging Windows from a marketing perspective and we are trying to copy Netscape and make IE into a platform. We do not use our strength -- which is that we have an installed base of Windows and we have a strong

> OEM shipment channel for Windows. Pitting browser against browser is hard since Netscape has 80% marketshare and we have < 20%. . . . I am convinced we have to use Windows -- this is the one thing they don't have. . . . We have to be competitive with features, but we need something more -- Windows integration. If you agree that Windows is a huge asset, then it follows quickly that we are not investing sufficiently in finding ways to tie IE and Windows together.... Memphis [Windows 98] must be a simple upgrade but most importantly it must be killer on OEM shipments *so that Netscape never gets a chance on these systems*." *Exhibit 19 (MS7 005526). (emphasis added)*

iv. *Microsoft Has A Dangerous Probability Of Success*

Microsoft's unlawful conduct creates a dangerous probability that Microsoft will succeed in misusing "monopoly power to beget monopoly." Microsoft already possesses a substantial position in the browser market. The latest data from a commercial market research firms shows that as of February 1998, Internet Explorer had a 58% share of the browser market, with Navigator at 40%. *Sibley Decl. ¶ 29 & Table 3.* Courts have found a dangerous probability of success when the defendant possessed a comparable share of the market. *See, e.g., McGahee v. Northern Propane Gas Co.*, 858 F.2d 1487, 1506 (11th Cir. 1988) ("[A] sixty or sixty-five percent share is a sufficiently large platform . . . to create a genuine issue of material fact as to whether [the defendant] would succeed in achieving a monopoly."); *Kelco Disposal v. Browning-Ferris Indus.*, 845 F.2d 404, 409 (2d Cir. 1988) (55% market share), *aff'd on other grounds*, 492 U.S. 257 (1989).

Microsoft's unlawful conduct will contribute to Internet Explorer's march toward dominance. Indeed, Microsoft *expects* that tying Internet Explorer to Windows is the lever that will inevitably enable it to prevail in the browser war. For example, when an internal debate arose within Microsoft about whether Memphis should be shipped without Internet Explorer 4.0, one Microsoft executive argued that it would be a "mistake" to ship without Internet Explorer because, among other things, "from all our research with IS and web professionals we know that they eventually expect us to win the browser war because IE will bundled with the operating system and they will have no real reason to purchase navigator." *Exhibit 37 (MS7 006063), K. Mehta 3/27/97 e-mail.* As explained by another Microsoft employee: "Leveraging our strong

share on the desktop will make switching costs high (if they get our technology by default on every desk then they'll be less inclined to purchase a competitive solution.)" *Exhibit 96 (MS7 002688-97).*

Moreover, the cumulative effect of the IAP and OEM restrictions described above is to significantly limit the means by which rival browsers may be distributed. Together with Microsoft's ICP agreements, the effect is substantially to foreclose the distribution of other browsers and quite possibly to tip the browser market toward Microsoft. *See Sibley Decl. ¶ 51*. As Dr. Sibley concluded, Microsoft's conduct, in the aggregate, thus "ha[s] an important independent effect on Microsoft's browser share." *Sibley Decl. ¶ 30*; *see also supra*, section IV.A.4. Accordingly, Microsoft's conduct, combined with Microsoft's existing market share, amply demonstrates dangerous probability of success. *Cf. Spectrum Sports*, 506 U.S. at 456 (dangerous probability of success presents "'a question of proximity and degree'" (quoting *Swift & Co. v. United States*, 196 U.S. 375, 402 (1905) (Holmes, J.).

D. The Balance Of The Equities Warrants Granting The Requested Preliminary Relief

The evidence and analysis set forth above amply demonstrates that the United States has shown a clear likelihood that Microsoft's ongoing and impending conduct violates Sections 1 and 2 of the Sherman Act. Accordingly, irreparable harm to the public interest in competition may be presumed. *See United States v. Siemens Corp.*, 621 F.2d 499, 506 (2d Cir. 1980); *cf. FTC v. Weyerhaeuser Co.*, 665 F.2d 1072, 1082 & n.22 (D.C. Cir. 1981). But this Court need not rest on the presumption. Microsoft's conduct threatens to work significant and irreparable harm to competition; the imposition of preliminary relief will eliminate this threat; the requested relief will not impose a significant burden on Microsoft and will benefit, rather than harm, third parties; and granting such relief is in the public interest. Accordingly, the Court should enter the requested preliminary injunction.

1. *Microsoft's Conduct Threatens Irreparable Harm To Competition*

Microsoft's unlawful conduct threatens irreparable harm to competition in two important respects. First -- and most important -- Microsoft's forced licensing of Internet Explorer, along with Microsoft's exclusionary agreements with IAPs and ICPs and Microsoft's restrictions on

OEMs' ability to alter the Windows desktop and boot-up screen sequence, inhibit competing Internet browsers from developing into full-fledged competitors to Microsoft's PC operating system monopoly. As explained above, the durability of Microsoft's monopoly is in large measure due to network effects that cause users to demand a ubiquitous operating system and that induce application developers to write for that platform. *See supra*, section IV.A.1(b)(2)*; Sibley Decl.*, ¶ *14*. By foreclosing the channels through which consumers obtain competing Internet browsers, and by entering into agreements that bias technological standards toward Internet Explorer, Microsoft substantially reduces the probability that competing Internet browsers can obtain sufficient market share to become an alternative platform to Windows and thereby break Microsoft's stranglehold on the operating system market.

Given the difficulty in overcoming the network effects that secure Microsoft's monopoly, the lack of direct competitive threats, and the extent to which Microsoft's ongoing and impending practices threaten to foreclose the major indirect competitive challenge to its monopoly, the threat to the public interest in competition is acute. As the Court has already once concluded, "the probability that Microsoft" through its unlawful conduct will "reinforce its operating system monopoly" "is simply too great to tolerate indefinitely until" this case "is finally resolved." *United States v. Microsoft Corp.*, 980 F. Supp. 537, 544 (D.D.C. 1997).

Second, Microsoft's unlawful practices threaten to garner for it "yet another monopoly in the Internet browser market." *Id.* Microsoft's practices, in the aggregate, substantially restrict the most important channels by which competing browsers might otherwise reach customers. Consequently, Microsoft's conduct threatens to weaken severely non-Microsoft browsers -- potentially to the point where the "browser market could tip to monopoly" in Microsoft's favor. *Sibley Decl.* ¶ *51*. And, once this occurs, "entry barriers" in the browser market "are likely to arise naturally, much as they do in the OS market." *Id.* "With IE dominating the browser market, websites will be written to the IE technology. This will induce more end-users to switch to IE, increasing software developers' incentives to build websites around IE." *Id.* The result will be an "opportunity" for Microsoft "to benefit from a less competitive market structure in the Internet just as it has in the OS market." *Id.* Accordingly, the Court's prior conclusion that Microsoft's "practices should be abated until it is conclusively determined that they are benign," *Microsoft*,

980 F. Supp. at 544, remains fully applicable here.

To be sure, Microsoft, threatened with a congressional inquiry and imminent litigation, unilaterally waived certain exclusionary restrictions in its agreements with ISPs and ICPs. But the most significant restraints on competing Internet browsers' access to the market remain. Microsoft, of course, steadfastly refuses to permit OEMs to remove Internet Explorer from the Windows 98 OEM Service Release. Nor has Microsoft abandoned its exclusionary agreements with Online Service Providers, companies which account for well over half of Internet access. Finally, even with respect to its agreements with ISPs and ICPs, Microsoft has not wholly relaxed its exclusionary restrictions. As discussed above, a Microsoft executive has testified that Internet Explorer must still account for at least half of each ISP's browser shipments.

Preliminary relief, therefore, remains urgently needed to ensure that Microsoft's remaining -- and most significant -- exclusionary conduct does not during the pendency of this litigation eliminate competition in the browser market and reinforce Microsoft's operating system monopoly.[58]

2. *The Requested Preliminary Relief Appropriately Preserves Competition*

The traditional function of a preliminary injunction "is to prevent irreparable injury." *Ross-Whitney Corp. v. Smith Klein & French Labs.*, 207 F.2d 190, 199 (9th Cir. 1953); *see also e.g.,Toledo AA & NM Ry. v. Pennsylvania Co.*, 54 F. 730, 741 (C.C.N.D. Ohio) (Taft, J.), *appeal dismissed*, 150 U.S. 393 (1893). *See generally* 11A Charles A. Wright *et al.*, Federal Practice and Procedure § 2948, at 137-38 (2d ed. 1995). The relief proposed by the United States is appropriately tailored to that aim.

The United States seeks as preliminary relief to enjoin Microsoft during the pendency of this action:

(1) from enforcing restrictive agreements which prevent OEMs, ISPs, and ICPs from choosing which browser or browsers they will distribute or promote, including any restrictions on the right of OEMs to remove Microsoft's browser or to implement

[58]Moreover, if the facts were to demonstrate that Microsoft -- which is "free to return to its old ways," *United States v. W.T. Grant Co.*, 345 U.S. 629, 632 (1953) -- might reimpose the restrictions it has unilaterally waived, preliminary relief as to those restrictions would be entirely appropriate as well. *See id.* at 633.

the OEM's own screen or boot-up sequence (Prayer ¶¶ 2a-d);

(2) from distributing a bundled version of its operating system and its browser at a single price unless Microsoft provides a practical way of removing browser functions and provides OEMs which do not wish to license the Microsoft browser an appropriate deduction from the royalty fee (Prayer ¶ 2f); and

(3) from distributing a bundled version of its operating system and its browser unless Microsoft treats Netscape's browser the same as its own with respect to inclusion and removal (Prayer ¶ 2e).

The first two categories of relief terminate Microsoft's illegal conduct. Granting such relief is essential because, as explained, Microsoft's conduct threatens irreparably to harm both consumers and competition.

Although suspending Microsoft's unlawful conduct during the pendency of the litigation is necessary to prevent irreparable harm to competition, it is not sufficient. Over the last several years, Microsoft has employed its unlawful licensing practices to secure for the Internet Explorer browser a substantial position in the market. Even if a substantial number of OEMs take advantage of the second form of relief -- and remove Internet Explorer and install a competing browser -- the advantage Microsoft has already unlawful acquired, coupled with the default inclusion of Internet Explorer with the copy of Windows 98 OEMs receive, means that the market might nonetheless tip toward monopoly in Internet Explorer's favor during the pendency of this suit. The result, of course, would be irreparable harm not only to competition in the browser market, but also to competition in operating systems as well.

Enjoining the release of Windows 98 would also prevent this harm. But that would deny consumers the benefits of Microsoft's new operating system software (quite apart from its browser functions). Thus, to avoid delaying the release of Windows 98, the United States seeks instead a prohibition on Microsoft's offering Windows 98 to OEMs unless it gives Netscape's browser equal treatment to that which Microsoft gives Internet Explorer. Netscape, of course, is the only browser positioned to prevent the market from tipping in Microsoft's favor.[59]

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[59]To the extent this relief could be viewed as mandatory, its imposition is amply justified by the threat to irreparable harm that Microsoft's forced licensing of Internet Explorer otherwise creates. *See,*

Finally, to ensure that the above relief is effective, the court should prohibit Microsoft from discriminating or retaliating in any manner against any person who chooses to exercise any of the above options or who refuses to license or distribute Microsoft's Internet browser.

3. *Preliminary Relief Will Not Impose A Significant Burden On Microsoft And Is Beneficial To Third Parties*

The proposed preliminary relief will not impose on Microsoft any significant burden, let alone inflict irreparable harm. The relief sought by the United States principally requires Microsoft simply to cease enforcing restrictions in its licensing agreements with OEMs, IAPs, and ICPs. As demonstrated, these restrictions are not supported by any efficiency justification and, therefore, prohibiting their enforcement will not cause Microsoft any harm. The third type of relief sought by the United States, equal treatment of Navigator, similarly imposes no substantial burden. Netscape has made its application software freely available, and for Microsoft to load another application onto the "master" CD-ROM on which it supplies Windows 98 to OEMs is a trivial matter that entails minimal costs.

Third parties -- far from suffering harm from the proposed relief -- will in fact greatly benefit. The relief proposed by the United States does not prohibit customers who wish to obtain Internet Explorer with Windows 98 from doing so. To the contrary, the proposed relief serves the interests of third parties, and the public generally, by creating greater consumer choice and by ensuring that competition on the merits, rather than Microsoft's monopoly power, determines which Internet browsers succeed. Moreover, the continued viability of non-Microsoft browsers, and thus the widespread distribution of the cross-platform JVM, will allow software developers to continue to take advantage of the benefits provided by platform independence. *See, e.g., Backes Declaration ¶¶ 5 - 8; Tierkel Declaration ¶¶ 6 - 8.*

4. *The Public Interest And The Balance Of The Equities Strongly Favor Enjoining Microsoft's Anticompetitive Practices*

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e.g., Toledo, 54 F. at 741 ("[I]t sometimes happens that the status quo is a condition not of rest, but of action, and that the condition of rest is exactly what will inflict the irreparable injury . . . . In such a case courts of equity issue mandatory writs before the case is heard on the merits."); *Aoude v. Mobile Oil Corp.*, 862 F.2d 890, 893 (1st Cir. 1988) (explaining that the doctrine that an injunction typically issue to preserve the *status quo* "is one of equity, discretion, and common sense, not woodenly to be followed").

Because the United States has a strong probability of success on the merits, and because the requested relief prevents irreparable harm to the public interest and imposes on Microsoft no significant burden, the balance of equities tilts sharply in the United States' favor. Accordingly, the court should enter the preliminary injunction.

What is at stake in this case, of course, is not simply that a monopolist might continue to impose unlawful restraints "until it is conclusively established that they are benign." *Microsoft*, 980 F. Supp. at 544. The reinforcement and extension of Microsoft's monopoly power threatens the competitive vigor of one of our most dynamic industries. The consequences may not be limited to eliminating competition among Internet browsers. Rather, the resulting maintenance of Microsoft's monopoly power is a long-term threat to the very innovation that is "the single most important force for improving productivity and national economic welfare." 3 Phillip E. Areeda, Antitrust Law ¶ 776c3, at 253 (rev. ed. 1996). Microsoft's anticompetitive conduct consequently should be enjoined to prevent further, and perhaps irreversible, competitive injury during the pendency of this case.

V. CONCLUSION

For the foregoing reasons, the court should enter the requested preliminary injunction.

Respectfully submitted,

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