IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF COLUMBIA

UNITED STATES OF AMERICA, Plaintiff, v. MICROSOFT CORPORATION, Defendant.	Civil Action No. 98-1232 (TPJ)
STATE OF NEW YORK *ex rel.* Attorney General DENNIS C. VACCO, *et al.*, Plaintiffs, v. MICROSOFT CORPORATION, Defendant.	FILED UNDER SEAL Civil Action No. 98-1233 (TPJ)

DIRECT TESTIMONY OF JIM BARKSDALE

INTRODUCTION

1. Since January of 1995, I have been the President and Chief Executive Officer of Netscape Communications Corporation ("Netscape").

2. I submit this written testimony in the consolidated matter of *United States v. Microsoft Corporation*, Civ. No. 98-1232, and *State of New York et al. v. Microsoft Corporation*, Civ. No. 98-1233 in accordance with the Court's Pretrial Order.

3. My statement will be presented in several sections below. Before moving into the more detailed discussions, however, I would like to state at the outset why I believe this case is so important not only for the software industry and the consumers of its products, but for the future of the Internet and electronic commerce. As I will detail in the pages to follow, Netscape is as innovative a company as exists. One of its founders, Marc Andreessen, is credited with being the inventor of the graphical browser, a software product which helped to open the Internet and the World Wide Web (the "Web") to consumers and to make possible the remarkable advances in electronic communications and commerce that have occurred in the four years since Netscape was incorporated. Through the extraordinary talents and efforts of its workforce, Netscape has created browser products, like the Netscape Navigator and the Netscape Communicator, which have won great critical acclaim and been extremely popular with consumers. However, because Microsoft Corporation

("Microsoft") determined that such products were a threat to Microsoft's Windows operating system software ("Windows") -- the software at the heart of over 90% of all personal computers in the world -- Microsoft set out to use its vast power as the producer of Windows to "cut off Netscape's air supply." It did this in a variety of ways, including, for example, by entering into exclusionary contracts and otherwise limiting Netscape's most important avenues of distribution for its software products; by refashioning its Windows software to disadvantage non-Microsoft browsers; by offering its browser product, Internet Explorer, at no cost and sometimes paying customers to switch from Navigator to Internet Explorer, even when Internet Explorer was intended for use with the Mac and UNIX operating systems ("OS") rather than Windows; and by unduly pressuring and intimidating Netscape's customers and potential customers.

4. I have been in business for many years, and Netscape and I know how to compete in a competitive marketplace. Microsoft's behavior over the last three years, however, indicates that the current software marketplace is not a competitive marketplace. Microsoft's monopoly control of the Windows OS software, and Microsoft's ability to improperly exercise the power associated with that control, allow Microsoft to cripple or cut off altogether innovative products that will benefit consumers if Microsoft deems those products to be too competitive with Windows or Microsoft's other software products. The

effectiveness of its power and its determination to use it became especially clear to me on two occasions during the last three years.

5. The first occurred in 1996. Compaq Computer Corporation ("Compaq") had decided to replace Internet Explorer with Netscape Navigator on a popular line of computers it shipped. Shortly after this decision was made, I heard that Microsoft threatened to cancel Compaq's Windows 95 license, which would effectively kill Compaq's OEM business. Although Compaq wanted to feature the Netscape Navigator icon on the desktops of Compaq computers, reflecting the popularity of the Netscape Navigator with consumers, Netscape learned that Compaq no longer intended to put Navigator on the desktop shortly after Microsoft threatened to cancel Compaq's Windows license. In this instance, Microsoft clearly used the power or its monopoly product to force a distributor to ship a separate new product. Thus, Microsoft was able effectively to destroy the value of Netscape's browser-distribution contract with Compaq, one of the world's largest PC manufacturers.

6. The second occasion was in October 1997, when I was present at a conference convened by Forrester Research Inc. ("Forrester"). The attendees at the conference consisted of approximately 200 corporate executives, many of whom were chief information officers. In connection with the presentations, the attendees were polled on several technology-related questions, and provided their answers through hand-held electronic devices. What struck

me was the response to the following question: "If Microsoft's Internet Explorer browser was not bundled free with Windows, would your company be less likely to use it?" Eighty-one percent (81%) of the 203 respondents to that questions answered "yes." Again, the power associated with the Windows franchise, and Microsoft's ability and willingness to abuse that power in the face of a threat from a popular and innovative competitive product, became crystal clear. This poll of corporate executives demonstrated to me how effective Microsoft had been by tying its monopoly product to its browser and giving away its browser, after spending hundreds of millions of dollars to produce and distribute it.

7. Throughout the duration of the governments' browser-related investigations of Microsoft's behavior, up to and including the events leading to this trial, Microsoft has tried to position Netscape as a "whiner" who can't compete in the marketplace. Nothing could be further from the truth. Netscape has shown an amazing ability to withstand the kinds of anticompetitive pressures Microsoft has put on it, and has been strong enough and innovative enough to re-invent its business model in the face of the slew of Microsoft actions designed to "cut off Netscape's air supply." I understand the pushes and pulls of competitive marketplaces; I understand that bullying and tough tactics do not necessarily violate any laws. But I also understand monopoly power and how it can be abused. My first job was as a salesman for IBM, and I learned

there through rigorous sales training that there is a legal limit, a place where bullying and tough tactics by a monopolist cross a line that should not and cannot be crossed. It is my view, based on what I have experienced and seen in the last several years, that Microsoft's behaviors have crossed that line.

8. I often ask people where browser technology would be today had Netscape not come along, and the response is uniform: it would be far behind where it is now. Many people have opined that, had Netscape not been willing and strong enough to look Microsoft in the eye and bring the browser to market, we would not have browsers (or anything like browsers) in the marketplace at all, meaning, of course, that the Internet and the Web would also not have developed as they have for widespread commercial and communications use. The software industry is watching this case closely, for if Microsoft is permitted to use its Windows-derived monopoly power to "cut off the air supply" of innovative products that threaten Windows and innovative companies that compete with Microsoft, there are few, if any, other companies that will try to do what Netscape has done. If this occurs, consumers and innovation will surely suffer.

9. The remainder of this statement will discuss more particularly various facts relating to this case. I will discuss these facts in two ways. In the first portion of the statement, I will discuss many of the facts in a summary form, without reference to specific exhibits or citations. Then, in the remainder of

the statement, I will discuss the facts in a more detailed way, complete with references to exhibits and citations. In these sections, my discussion of the facts will be organized in the following manner:

i. I will begin with Netscape's early history, including a discussion of my background as well as that of the founders of the company, Jim Clark and Marc Andreessen; a discussion of Netscape's highly successful development and marketing of browsers; a discussion of how the development of browsers led to the commercialization of the Internet and the Web; and a discussion of how the Netscape browser, as well as the Java programming language developed by Sun Microsystems, Inc. ("Sun"), posed a threat to Windows.

ii. I will then discuss Microsoft's responses to the success of Netscape and its browser products, including a discussion of Microsoft's efforts to divide the market and, when those efforts were not successful, Microsoft's various exclusionary, restrictive, and predatory actions undertaken to harm Netscape and its products, including actions designed to foreclose our access to key channels of browser distribution: Internet Service Providers and Online Service Providers (collectively, "ISPs"); Original Equipment Manufacturers ("OEMs"); Internet Content Providers ("ICPs"); Independent Software Vendors ("ISVs"); and actual and potential corporate customers ("Corporate

Accounts").

iii. Finally, I will discuss the consequences to Netscape and its browser products, as well as to the marketplace and consumers, of these harmful actions by Microsoft, as well as my thoughts on the essential elements of any remedy that would restore competition and consumer choice to this market.

SUMMARY OF FACTS

10. **Broswers and Netscape: New Frontiers** -- One of Netscape's co-founders, Marc Andreessen, conceived of the graphical browser while he was a computer science student at the University of Illinois. In 1993, he and a team of fellow students at the University of Illinois did the software development work necessary to translate Marc's vision into reality, and the University of Illinois then distributed the browser, under the name "Mosaic," for non-commercial uses over the Internet. The concept of the graphical browser was an important technological breakthrough; before the graphical browser, those using the Internet could not easily exploit the multimedia potential of the Web. Moreover, before the invention of the browser, users of the Internet tended to be limited to those with sophisticated computer skills, such as academics, university students, and industry and government researchers. As word of the Mosaic browser spread, however, a growing

number of people who were not heavy computer users also found they were able to browse the Web.

11. By the time Marc left the University of Illinois to move to California, he was aware of the commercial potential for the browser. He had seen the excitement that followed the introduction of his Mosaic browser, and knew there was already an unfulfilled demand for commercial browser licenses. He had also begun to think about related Internet-oriented software products with commercial usefulness. At about the same time, Jim Clark, Netscape's other co-founder, also began to focus on the commercial potential of the Internet. Their shared vision about the commercial significance of the Internet led Marc and Jim to co-found Netscape in April 1994.

12. The engineers at Netscape, including most of the team that had developed the Mosaic browser, created an entirely new browser between the time of the founding of Netscape and the end of 1994. This new browser, called Netscape Navigator, revealed new advances in browser technology that further hid the technological complexities of the Internet from the end user. Its introduction into the marketplace had a profound effect; the product was an immediate and huge success precisely because of its ease of use and its ability to bring so much new multimedia information to the consumer.

13. With the extremely rapid growth in the number of Netscape Navigator users, the Web itself exploded with new activity as individuals and businesses

scurried to set up websites that would draw traffic from the ever-expanding "Web community." Entire new job categories, such as those of "webmaster" and "Internet publisher," came into being to meet the need for individuals with Internet software knowledge and experience. Companies throughout the world began looking at the possibilities of electronic commerce and communications. In other words, Netscape's browser helped to open a huge new commercial frontier: the Internet.

14. Today, the Web constitutes a growing marketplace for the buying and selling of goods, services, and information ranging from automobiles to vacation rentals to out-of-print books and recordings. A recent report on the Emerging Digital Economy issued by the Department of Commerce projects that by the year 2002, the Internet may be used for more than $300 billion worth of commerce between businesses. By virtue of the Web's popularization, millions of people now often read their morning newspaper from their computer screen, which allows for the scanning of large amounts of information in a short period of time. Indeed, consumers can now receive late-breaking news updates without specifically seeking them out. Such is the new information driven world, a world that was brought to consumers and adopted by millions as a result of Netscape's commercialization of its web browsing and other related Internet technologies.

15. One of the new job categories that was spawned by the introduction of the

browser was that of Internet software developer. This job category has become increasingly important with the growing realization that the browser is not only useful for browsing the Web but also can serve as a platform for the development of all sorts of network-centric software applications, such as online-banking software products. These network-centric applications, in essence, sit on top of the browser and take advantage of its Web-oriented functionality. In addition, the widespread distribution of Netscape Navigator facilitated widespread distribution of the Java programming language developed at Sun Microsystems. Java allows software developers to write cross-platform applications that will run on any operating system, increasing consumer flexibility and ease of use, while reducing development costs associated with writing an application and then porting it to run on various different operating systems. For businesses that utilize many different operating systems (for instance several versions of Windows, the Macintosh operating system, and UNIX), this ability to implement cross-platform applications can substantially reduce software support and training costs. Netscape's browser, using Java, provided both the technical means and the broad distribution to offer a new "super-platform" for developers of network-centric applications. This platform aspect of the browser, and the cross-platform benefits of Java, allowed for the development of software applications that were directed more to the Internet than to the desktop, and

thus had the potential to serve as a partial substitute for the Windows OS as a development platform.

16. Netscape's browser products received a tremendous amount of mainstream press coverage. This press coverage, combined with Netscape's marketing efforts, helped foster what became the Internet "phenomenon." Since the introduction of Netscape's browser, productive use of and access to the Internet are advocated by well respected business people, such as Bill Gates, and have become the mantra of many well known political figures, including Vice President Al Gore. Because the Internet opened up a whole new world of possibilities for every consumer and business person alike, the entire computer industry was revitalized.

17. Although Microsoft very recently has tried to suggest that its own corporate Internet strategy dates back to April 1994, this is inconsistent with prior statements of Microsoft executives, including Bill Gates. On December 7, 1995, Mr. Gates indicated that the Internet phenomenon had caught Microsoft by surprise. Indeed, according to a report in Newsweek magazine, Microsoft had only 4 people working on developing a browser in January 1995. It was not until May 1995 that Mr. Gates told his executive team, "Now [emphasis added] I assign the Internet the highest level of importance." (Newsweek, "The Browser War" April 29, 1996, p. 47). Microsoft, like many other companies, began revising its business plans to

take into account the advantages of Internet technology. Unfortunately, unlike other companies, Microsoft's new business plans also included plans for how to eliminate Netscape as a competitor because of the threat the browser posed to Microsoft's Windows monopoly. As I later discuss, those plans included tactics designed to use Microsoft's monopoly power not only to defeat Netscape but, using an "embrace and extend" model, to extend the proprietary Windows technology ultimately to the Internet itself.

18. **Netscape's Early Business and Distribution Successes** – Capitalizing on the burgeoning electronic-commerce marketplace and the development of platform-independent software, Netscape rapidly enjoyed great success in the distribution and use of its browsers and in the revenues it received from browser licensing. The commercial release of Netscape Navigator 1.0 occurred on December 15, 1994. By the end of the second quarter of 1995, Netscape had collected over $10 million in revenue generated by the browser alone. By the end of 1995, Netscape had collected approximately $45 million in revenue from browsers. Given the young age of the company, these numbers are significant standing alone. However, what is even more significant is that Netscape generated this kind of distribution and revenue with a very small staff of order takers, reflecting the strong demand for our product.

19. Netscape was also successful in opening a variety of distribution channels.

First, Netscape was able to sign up many of the world's largest OEMs in 1995. The OEM distribution channel was important to Netscape's continuing success because people were buying computers to get connected to the Internet. Thus, a browser installed on a new machine purchased by a new computer owner was very likely to continue to be used by the new user. Second, Netscape was able to establish a large number of relationships with ISPs. ISPs provided the mechanism through which people could actually get connected to the Internet. Clearly, a user who is signing up with an ISP is doing so to be able to access information on the Internet. As with OEM distribution, if a user obtains a browser in conjunction with signing up with an ISP for Internet access, that user is very likely to adopt and stay with the browser distributed by the ISP. Netscape was also very successful in the area of direct sales to corporations, direct retail sales to consumers, and through downloading via the Internet.

20. Although Netscape distributed the beta (i.e., pre-release) version of Netscape Navigator 1.0 free on the Internet, Netscape's business model in the early days reflected our intention to charge customers to use the browser. Consistent with this intent, soon after Netscape rolled out its retail release on December 15, 1994, Netscape made it clear to the world that Netscape would charge for Navigator. The initial price for a Navigator license was $39. With regard to the consumer market, Navigator was available for a free trial

download for a limited (90-day) period, but the Navigator license explicitly required consumers to pay for the browser after the evaluation period. As Netscape's browser revenues reflect, customers did pay. With regard to the enterprise, OEM, and ISP markets, Netscape always charged a significant fee for its browser -- even in situations where the purchaser intended to distribute Navigator for free to its customers -- such as in the ISP market. The only exception built into Netscape's pricing structure was to provide the browser free to the education and non-profit market. Even in this area, Netscape's plans with regard to distribution of the browser had a profit motive: educational users who liked the product would want to use it when they entered the business market, and such distribution built strong brand awareness that was certain to have positive economic effects in the future.

21. Netscape's revenue growth in 1995 was so great that the company was named the fastest-growing software company in history. During this phase of growth, we continued to build out the infrastructure of our business, adding new employees, new programs for software developers, new marketing programs, new sales offices, and, of course, continuing to focus on building great Internet software. Our employee base grew from approximately 100 people at the end of 1994 to approximately 500 people by the end of 1995. In 1995, we received more than 20 product awards for Netscape Navigator. And in 1995 we completed a highly successful IPO.

22. **Microsoft's Response: Play Ball or Else** – As stated above, Microsoft did not fully appreciate the shift represented by the Internet phenomenon until after the debut of Netscape Navigator in late 1994. One of the first steps Microsoft took in response to its growing appreciation of the significance of the Internet was in December 1994, when it obtained a license to use and redistribute the Mosaic browser code originally developed by Marc Andreessen and his team of fellow students. This license came from a company, Spyglass, that had obtained rights to the code from the University of Illinois. Based on press reports, Microsoft agreed to pay Spyglass royalties for the Mosaic code, and expected to use this code as the basis for its own commercial browser product.

23. During this same time period, Microsoft and Netscape engaged in a number of conversations, including discussions relating to technical standards issues and efforts to explore a possible cooperative arrangement between the companies. This goal seemed reasonable enough; what I did not imagine at the time, however, was that Microsoft's actual goal was to attempt to convince Netscape not to compete for the vast majority of the browser business -- the business related to the Windows 95 platform -- and to destroy Netscape's business if it refused to agree not to compete.

24. Although my meetings and discussions with Microsoft prior to our June 21, 1995 meeting seemed as if they might be productive, I was concerned about

Microsoft's possible motives and Microsoft's ability to severely impede Netscape's ability to compete if Microsoft chose to use its monopoly power in the operating system market. Unfortunately, as I learned on June 21, these concerns were justified.

25. At the June 21 meeting, I experienced something I had not ever seen happen in my more than thirty years of experience with major U.S. corporations, including IBM, Federal Express, and McCaw Cellular Communications. Microsoft, led by Dan Rosen, came to Netscape under the guise of attempting to set up some sort of cooperative agreement with Netscape. However, rather than proposing potential productive areas of cooperation, Microsoft apparently came to Netscape with a single focus: to convince Netscape not to compete with its Windows 95 browser product, Internet Explorer. Microsoft proposed a division of the browser market between our companies: if Netscape would agree not to produce a Windows 95 browser that would compete with Internet Explorer, Microsoft would "allow" Netscape to continue to produce cross-platform versions of its browser for the relatively small market of non-Windows 95 platforms: namely, Windows 3.1, Macintosh, and UNIX. Moreover, Microsoft made clear that if Netscape did not agree to its plan to divide the browser market, Microsoft would crush Netscape, using its operating system monopoly, by freely incorporating all of the functionality of Netscape's products into Windows. Several other issues were discussed in the

meeting, including technical specifications that Netscape needed to make its browser compatible with the upcoming Windows 95 release (assistance that Microsoft normally provided to ISVs such as Netscape), the possibility that Netscape would adopt certain Microsoft technologies and that Microsoft would adopt certain Netscape technologies, the possibility of Netscape becoming what Microsoft called a "preferred" solutions provider, and the possibility of Microsoft taking an equity position in Netscape. Near the end of the discussions, I asked Dan Rosen if Netscape's ability to obtain necessary technical specifications was conditioned on agreeing to Microsoft's proposal to divide the market and take an equity position in Netscape. He said that "It certainly isn't independent."

26. I left the meeting stunned that Microsoft had made such an explicit proposal. And I was surprised at the degree of threat to the Windows monopoly apparently perceived by Microsoft, especially because Internet Explorer product had not yet even been introduced and would not be introduced until after the release of Windows 95. Moreover, Netscape Navigator was a software application with platform characteristics, but it was not an operating system, like Windows. Given these facts, Microsoft could only have had one goal: to obtain and control a significant proportion of the future growth of the Internet.

27. **Microsoft Makes Good On Threats** -- Netscape refused Microsoft's

proposal and prepared itself to deal with Microsoft's threats. But I did not anticipate the extent to which Microsoft would use its monopoly power over operating systems to take specific actions designed to destroy Netscape's ability to compete in the browser marketplace -- or at a minimum, to so disrupt our browser-generated revenues that it would impede our ability to continue to pose a competitive threat.

28. On December 7, 1995, Microsoft announced its Internet strategies. Bill Gates told the world that Microsoft's browser would be given away for free, and to the reported glee of Microsoft's executives, Netscape's stock price fell almost $30 per share. I knew that Microsoft would incur considerable cost in developing and distributing its browser, but I also knew that Microsoft's overwhelming share of the operating system and office-suite software market provided Microsoft such enormous resources that it could make good on its announced plan. What I subsequently experienced was that Microsoft not only gave away its browsers for free; it actually, in effect, ended up paying many customers to license Internet Explorer instead of Netscape Navigator. In 1996 and 1997 I learned of repeated instances of Microsoft providing free products, free services, free advertising, and even in some cases substantial financial payments for each copy of Netscape Navigator removed from an installation and replaced by the free Internet Explorer. Even though Netscape constantly revised its pricing structure, it was impossible to stay

competitive with "better than free." These actions also threatened Netscape's ability to continue to innovate. As Microsoft was well aware, Netscape's business model depended on browser revenue. Cutting off Netscape's browser revenue would mean Netscape would not have dollars to funnel back into continued product development, as Bill Gates announced to the Financial Times of London in June of 1996.

29. On December 7, 1995, Microsoft also publicly announced that it would be bundling its browser into with its Windows operating system. Analysts noted at the time that, given that there were over 100 million users of Windows software, Netscape's ability to distribute its browser would be key to its ability to compete with Microsoft. Recognizing the importance of distribution to Netscape, Microsoft then began to use its market power to extract exclusionary deals with many of the largest OEMs and ISPs -- the two most significant Internet software distribution channels in the maturing market.

30. With respect to the OEMs, Microsoft made clear through its words and actions that PC computer manufacturers should not get too close to Netscape or there could be negative consequences in their dealings with Microsoft. This was a serious matter for those OEMs; without a Windows license, and without cooperation from Microsoft in general, their P.C. businesses are worthless. Netscape had signed distribution contracts with a number of these OEMs in 1995, but during 1996, as Microsoft became more aggressive

in its efforts to slow down the distribution of Netscape Navigator, it became increasingly difficult for Netscape to get its products effectively distributed through this channel. For OEMs, like Compaq, that wanted to delete the desktop icon for Internet Explorer and put a Netscape Navigator icon on their computer screens, (reflecting the popularity of the Netscape browser, and thereby increasing the value of the PC), Microsoft threatened to terminate their Windows licenses, which would have put them out of business. Microsoft also offered a variety of financial incentives to these OEMs to "prefer" Internet Explorer over Netscape Navigator, including reductions on license fees for various Microsoft software products. In 1996 Microsoft imposed a new license restriction on the OEMs, one requiring that the first, or "boot-up," screen be controlled by Microsoft rather than the OEM, so that, as Steve Ballmer, Microsoft Executive Vice President, told Forbes magazine, Netscape's browser would not be able to take over the desktop.

31. With respect to the ISPs, Microsoft again entered into restrictive contracts and offered a wide range of financial incentives in exchange for the commitment of the ISP to "prefer" Internet Explorer over Netscape Navigator. Microsoft's campaign to limit Netscape's access to the ISP channel was especially strong with respect to the larger and more visible ISPs, such as America Online ("AOL"), who were offered placement on the Windows desktop in exchange for exclusionary treatment of Netscape's

browser. As I learned from Steve Case of AOL, this placement on the Windows desktop was extremely valuable to the ISPs; it meant they had immediate access to Windows users – who constitute over 90% of PC computer users – without incurring the substantial hard-dollar costs associated with other distribution methods. Given Microsoft's extensive investment in Microsoft Network ("MSN"), its own on-line service offering, the offer of desktop placement to competing online service providers like AOL was particularly revealing about how seriously Microsoft took the Netscape browser's threat to the Windows monopoly.

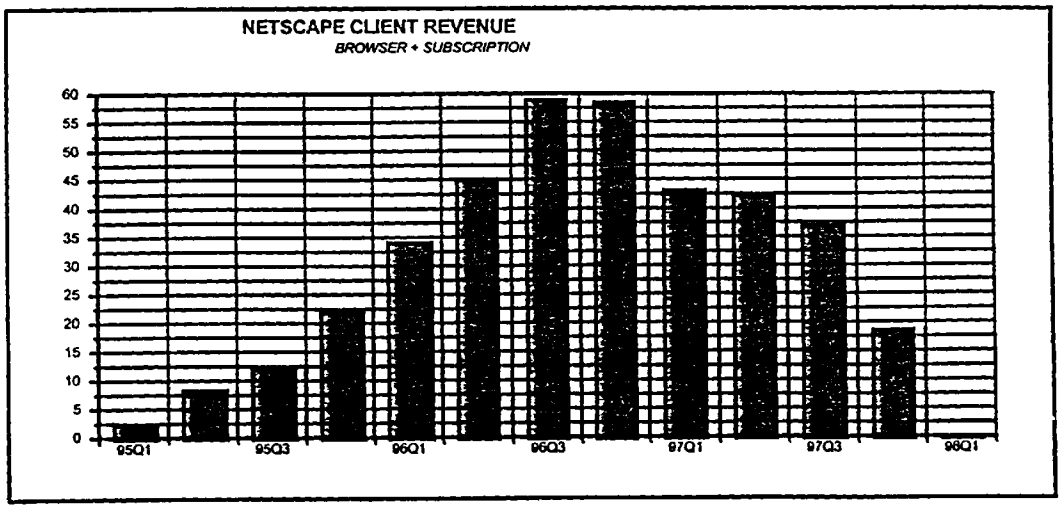
32. It is important to understand why distribution through the OEM and ISP channels is so important. Less sophisticated computer users in particular are much more likely to use the browser that comes on their computers, or that comes as part of their Internet access service, than to download from the Internet. OEM and ISP distribution constitutes the primary means through which most users -- particularly home and unsophisticated users -- have gotten their browsers in recent years. Moreover, once a user starts with a given product, he or she tends to stick with that product. This means that if a new user is not presented with a choice of browsers at the time they buy a new computer or subscribe to an ISP service, and are offered only Internet Explorer, it becomes that much more difficult to convince them at a later time even to try the Netscape browser. In comparison with the OEM and ISP

channels, other methods of distribution, while obviously important, are less valuable. For example, while Netscape achieved some of its early success through distribution by downloading from the Internet, and necessarily continues to rely heavily on this channel of distribution, downloading today can take a long time to complete and requires some level of computer knowledge and sophistication. Another frequently referenced method of distribution of software is through large-scale, unsolicited mailings of computer disks ("CDs"), a method referred to as "carpet bombing." Carpet bombing is disproportionately expensive for a company, like Netscape, that does not have an expectation of a future stream of associated monthly usage fees to offset the cost. Similarly, retail distribution of a free software product is economically impractical.

33. Microsoft also engaged in other predatory acts designed to prevent Netscape from competing in the browser market. I began receiving reports of technical problems that resulted from using Netscape in conjunction with certain Microsoft products and in conjunction with accessing certain Web sites. Microsoft also made it difficult for Netscape to license certain important technologies -- although it made those same technologies available to other developers for free. The preceding list of Microsoft practices is by no means an exhaustive list -- simply a summary of actions to be detailed below.

34. **Effect of Microsoft Conduct on Netscape and Consumers** – Microsoft's

anticompetitive practices directly affected Netscape's ability to compete. These effects manifested themselves in many forms. The most significant include a marked decrease in Netscape's browser market share over time, as well as a marked decrease in our browser revenue over time, leading to its ultimate elimination this year. In the first quarter of 1996, before Microsoft's practices began having their intended effects, Netscape had over 70% of all browser users and derived approximately 70% of its license revenue from client licenses. The following graphic depicts Netscape's browser revenues over time, and demonstrates the affects of Microsoft's practices on Netscape:



35. Given the nearly exponential growth of the Internet, if Microsoft had not engaged in its anticompetitive practices, it is my belief and was the expectation of Netscape that Netscape would have been able to continue on its mid-1996 trajectory. However, Microsoft's practices had dramatic and

direct results. By October of 1998, Netscape's market share is estimated to be somewhere between approximately 40% and 50%, depending on the market segment considered, and it now derives 0% of its revenues from browser licensing. These market share effects are felt most dramatically with regard to new home users, who generally acquire their browsers through purchasing an OEM built computer or through their ISP. According to a September 1998 study by IDC, Netscape's market share for new home users has declined from 51% in 1996 to 35% in 1998.

36. Moreover, consumers are directly affected by Microsoft's practices. By trying to destroy innovative companies like Netscape, Microsoft has sent a message to the industry -- if Microsoft perceives that your success has the potential to undermine Windows in any way, Microsoft will do everything in its power to destroy you. The end result is reduced innovation, and thus, fewer choices for consumers.

37. Microsoft alleges that Netscape lost market share to Microsoft because Microsoft improved the quality of its products to a level exceeding that of Netscape's products. While Microsoft did improve its products over time (as did Netscape), this improvement did not result in the loss of market share -- and revenue -- that Netscape has endured since Microsoft began its pattern of anticompetitive practices. As of the 1.0 and 2.0 releases of Netscape Navigator and Microsoft Internet Explorer, it was clear that the industry and

consumers perceived the Netscape product as superior in every way. As of the 3.0 releases of both products, Netscape's product was still perceived by most as the superior product. As of the 4.0 releases of the products, the best that can be said for Microsoft is that the Netscape product and the Microsoft product have some level of parity of features and functionality. Even with regard to the 4.0 releases, however, Microsoft's reviews have suffered because of its lack of stability. Thus, even if Microsoft's products and Netscape's products were considered to be equivalent, such parity does not and could not explain the marked reduction in revenue and market share that Netscape suffered as a result of Microsoft's exclusionary and other anticompetitive practices. Based on the reports of Microsoft's practices I was hearing every day, combined with the empirical loss of revenue Netscape suffered as a result of Microsoft's practices, it would not have been totally outrageous for Netscape to do exactly what Microsoft wanted: stop innovating with our browser product. However, we did not do so and, as stated above, at best the current reviews give the Netscape and Microsoft browser offerings similar ratings.

38. **Remedy** – Based on the practices that my company and I have experienced in the last three years, and based on my understanding of Microsoft's ability to and current practice of distributing Internet Explorer separately from its operating system products (which it does for use with other operating

systems), I believe that an appropriate remedy would be to order Microsoft to distribute Internet Explorer separately from its operating system products and to prohibit Microsoft from entering into exclusionary contracts relating to distribution of Internet Explorer. In particular, one of the consumer advantages that Microsoft uses to argue in favor of its so-called "integration" of the browser and the OS is the ability of its browser to browse information located on distant sites (such as the Internet) and on local sites (such as a computer's hard drive) in a consistent fashion. This, however, as well as a host of other advantages that Microsoft claims to have achieved by "integration," does not justify what Microsoft calls its "integration" of the OS and the browser, because the Netscape browser, when installed on Windows, is capable of accomplishing most if not all of the same tasks with the same benefits.

39. While the situation is not beyond recovery, it is critical to have relief from Microsoft's foreclosure of distribution and other predatory acts as soon as possible. Microsoft's actions have stifled competition, which ultimately threatens innovation and lessens the likelihood that consumers will have a free choice to select the products they want at the lowest possible price.

DETAILED DISCUSSION OF FACTS

MY BACKGROUND

40. I graduated from the University of Mississippi in 1965 with a degree in Business Administration. By the time I graduated from the University of Mississippi, I had set my sights on IBM as my first employer. I worked in sales at IBM from 1965 until 1972, first as a salesman in the Memphis office, and then in a staff position in Princeton in IBM's finance industry market. During my time at IBM, the IBM culture and training programs focused extensively on developing customer relationships, customer service, and acceptable business conduct, namely ethics and how to treat customers with respect. The training I received at IBM substantially shaped the way in which I do business -- even today.

41. I left IBM in 1972 to work with a group of friends starting a business focused on buying, selling, and leasing used IBM computers. The company was called Econocom and was a subsidiary of Cook Industries ("Cook"). Later, I handled the data processing for the entire Cook enterprise, which at the time encompassed a variety of businesses varying from real estate to commodities to agricultural chemicals. In the late 1970's, Cook sold off its data processing division to Federal Express, which was just starting out in Memphis. I stayed at Cook for another six months, as President of its insurance subsidiary.

42. In 1978, I was recruited by Federal Express to run its Management Information Group. I joined Federal Express as a Senior Vice President, and I ultimately became Executive Vice President and Chief Operating Officer at Federal Express, a company that then employed 90,000 people worldwide. Under my direction, my team built the largest single-image IBM Information Management System in the world. The Federal Express Information Management System tracked airplanes, trucks, vans, and the parcels themselves. Based on the system my team developed, I believed Federal Express could be thought of as a systems company that happens to be in the transportation business. The Information Management System essentially was a communications network. During my tenure, I acquired necessary communications equipment, such as private radio networks and all-digital dispatch systems, and linked them to the computer system in a way that allowed any customer to call in at any time and track the status of a package using a simple tracking number. My Federal Express experience allowed me to gain valuable experience in developing an extensive communications network from the ground up. While I was Executive Vice President and Chief Operating Officer from 1984 to 1991, Federal Express' sales grew from $1 billion to $7.7 billion, and its operations expanded to 135 countries.

43. I was recruited from Federal Express in 1991 to join McCaw Cellular Communications ("McCaw"). At McCaw, I had the opportunity to participate

in the development of another extensive communications network. Prior to the time I joined the company, Craig McCaw, founder of McCaw Communications, had taken a step that many thought was crazy. Because he foresaw the coming of age of the wireless communications industry, Mr. McCaw borrowed almost $5 billion to finance a national cellular network. I started as President and Chief Operating Officer at McCaw during a critical expansion period for the company. I believed the wireless communications industry had tremendous potential given the growing popularity of all types of wireless communications -- cellular phones, pagers, fax machines, and wireless e-mail -- and that Mr. McCaw had made the right decision. McCaw grew at an incredible rate, and in 1994, AT&T purchased McCaw for $11.5 billion. I was recruited from McCaw to become Netscape's President and CEO shortly after McCaw was acquired by AT&T.

44. I first became interested in Netscape after reading an article about the company in a July 1994 article in Fortune magazine entitled "25 Cool Companies." Soon after I saw the article, Jim Clark, now-Chairman of Netscape, and John Doerr, of Silicon Valley's premier venture-capital firm, Kleiner Perkins Caufield & Byers, came up to Seattle, where I was then living, to meet with me. Doerr had just offered to help fund Netscape, and his company was highly regarded for putting together top-notch management teams for the companies it chose to fund. I was still with McCaw and didn't

want to take on any new commitments until McCaw's merger with AT&T was completed, but I did agree to become a member of Netscape's board of directors. I joined the Netscape Board of Directors in October 1994.

45. As I served on Netscape's board of directors, I saw many ways that Netscape's software could help improve business processes and communication. I decided to accept Jim Clark's offer to lead the company, and on January 16, 1995, I became president and chief executive officer of Netscape.

46. After having worked for two brilliant, dynamic entrepreneurs -- Fred Smith at Federal Express and Craig McCaw of McCaw -- both of whom I admired and learned a lot from, I wanted to have the chance to run my own start-up. The excitement surrounding Netscape in 1994 and 1995 is now legendary. The company's flagship product, Netscape Navigator, helped the Web to explode in popularity and fueled the Internet revolution, growing from more than 2 million users by the end of 1994 to 15 million users just one year later.

HISTORY OF NETSCAPE

47. Netscape was founded in 1994 by Jim Clark and Marc Andreessen. Clark had previously founded Silicon Graphics, Incorporated ("SGI"), a successful start-up that had grown into a multi-billion-dollar Fortune 500 company renowned for its innovative, high-end computer graphics workstations. Among other things, Silicon Graphics workstations were used to design

everything from special effects for Hollywood movies to sophisticated industrial products.

48. Andreessen and a team of fellow students from the University of Illinois at Champaign-Urbana had created the first graphical Web browser, called Mosaic, in 1993 at the National Center for Supercomputing Applications ("NCSA"). The Web's popularity grew substantially after the release of Mosaic. The innovative Mosaic was not only the first browser with a graphical user interface, but it was also the first graphical browser to be available on the Microsoft Windows and Macintosh platforms.

49. Clark, a former University of California and Stanford engineering professor, was intrigued by the possibilities of the Internet as a vehicle for interactively delivering data, so in 1994 he e-mailed Andreessen, who had recently moved to Palo Alto, California, and the two met over the course of a few weeks to work out the idea and the details of the new company. The company was incorporated on April 4, 1994.

50. Netscape hired most of the original NCSA Mosaic engineers, plus a few new additions, including Lou Montulli, who had invented the Lynx text-only browser, and established its offices in Mountain View, California. The engineers set to work to create an original browser and server that were faster, more secure, more stable, and more feature-rich than any other products then on the market. Tom Paquin, a skilled engineering manager at

SGI, soon joined the team to manage the engineers.

51. Meanwhile, the talented Netscape engineers were dedicated to logging long hours at their computers to create Netscape's groundbreaking new browser. A beta version of the company's first product, Netscape Navigator 1.0, was distributed over the Internet on October 13, 1994.

52. Netscape was the first commercial company to distribute its software over the Internet. Now, a mere four years later, nearly all major software vendors routinely make their products available for download on the Internet. While software distribution on the Internet was once viewed as an unusual idea, it is now commonplace, and Netscape is the company that pioneered it.

53. Toward the end of October 1994, Netscape became a founding member of the World Wide Web Consortium ("W3C"), the Internet standards body created by the Massachusetts Institute of Technology to establish international standards for client and server software. Open-standards products enable global online commerce and communications over the Internet and give consumers multiple choices when they shop for software. Netscape has always been a leader in creating interoperable, open standards products that work across a range of client and server platforms, legacy systems, databases, and non-PC devices. Our engineers are continually working on developing new, useful open standards; in fact, we count among our employees Kipp Hickmann, one of the inventors of Secure Sockets Layer ("SSL"), a security

protocol; Brendan Eich, the inventor of JavaScript, which was standardized under the name ECMAScript; Tim Howes, co-author of the Lightweight Directory Access Protocol ("LDAP"); and John Myers, who worked on the Internet Message Access Protocol ("IMAP"), version 4. The original Netscape Navigator and Netscape server teams also pioneered the use of Internet standards, making their products backward-compatible with all existing Web browsers and servers.

54. The final version of Netscape Navigator 1.0 was released on December 15, 1994. The product delivered many times the performance of other browsers available at the time. Its innovative capabilities included continuous document streaming, enabling users to interact with documents while they were still being downloaded rather than waiting for the entire document to load; multiple network accesses, allowing several documents or images to be downloaded simultaneously; native support for the JPEG image format; and security features such as encryption and server authentication. It was available for the Microsoft Windows, Macintosh, and Unix operating environments. The single-user price of the software was $39; volume discounts were available. Netscape Navigator enabled the Internet to be used by those who were not long-term or experienced computer users. In other words, it opened up the Internet for use by anyone.

55. Netscape's first two server products, Netscape Commerce Server 1.0 and

Netscape Communications Server 1.0, were also released on December 15, 1994. The Netscape Commerce Server, incorporating SSL technology, was the first secure server software available for the Internet. Netscape Communications Server was used by online publishers.

56. By the end of Netscape's first year of business, the company had Digital Equipment Corporation ("Digital") on board as the first reseller partner of the company's server software and counted such major enterprises as Bank of America, MCI, and First Data as customers. Both First Data and Bank of America used Netscape software to provide real-time online credit card authorizations for their customers, giving businesses a secure way to conduct electronic commerce on the Internet. MCI used Netscape Navigator and Netscape Commerce Server software as a turnkey solution for companies and consumers to conduct business on the Internet.

57. Demand for Netscape's products was enormous and unprecedented. In 1995, we were named the fastest-growing software company in history. In the first quarter of 1995, we received $2.3 million in license fees for Netscape Navigator. By the fourth quarter of 1995, license fees for Netscape Navigator had shot up to $21.7 million. License fees for Netscape Navigator for the entire year totaled $44.3 million, which accounted for more than half of our 1995 annual revenues of $85.4 million.

58. The exploding marketplace for Netscape's products woke Silicon Valley up

and generated intense developer interest in the Internet. Hundreds of Internet-oriented start-ups seemed to spring up overnight, and even large, established technology companies looked for ways to address the Internet in their businesses. It was an exciting time to be in Silicon Valley, witnessing the birth of a new industry -- the Internet industry. It reinvigorated everyone.

59. Driven by a vision we all believed in, everyone at Netscape was dedicated to making the company -- and the Internet industry -- succeed. By integrating our own Internet products into our business processes, we were able to increase productivity, gain a quicker time to market, and turn out innovative new products in what first came to be known as "Netscape time," and now is known as "Internet time." Led by Netscape, the cycle for developing new software shrank from two years to half a year.

60. Netscape grew from about 100 employees by the end of 1994 to approximately 500 employees by the end of 1995. Excited by the opportunities of the Internet industry and the innovations we were creating, the best and the brightest were beating down the doors to come work for Netscape. As the company grew, it was rewarding to see how much fun Netscape employees had doing something that they knew was relevant and important.

61. In 1995, Netscape introduced a number of new products, including Netscape Navigator 2.0, Netscape Navigator Gold 2.0, and Netscape Power Pack 1.0, a

suite of add-on applications that extended the capabilities of Netscape Navigator for Windows. The company added Netscape Mail Server, Netscape News Server, and Netscape Proxy Server to its server product line, complementing the existing Netscape Commerce Server and Netscape Communications Server products. Netscape also shipped its first development tools, Netscape LiveWire and Netscape LiveWire Pro, and its first electronic commerce products, Netscape Internet Applications.

62. Netscape Navigator won more than 20 product awards in 1995. Netscape Navigator Personal Edition, a new product, reached No. 1 on Ingram Micro Devices communications software bestseller list just four months after debuting in the retail channel.

63. In April 1995, Netscape announced that it had concluded a private placement of Series C preferred stock with leading companies in the publishing and technology industries. Adobe Systems Incorporated, The Hearst Corporation, Knight-Ridder, TCI Technology Ventures, and The Times Mirror Company took an 11 percent minority stake in the company during the financing round. Morgan Stanley & Co. Incorporated, acted as placement agent for the investments.

64. On August 9, 1995 Netscape completed its initial public offering of 5,000,000 shares of its Common Stock at a price of $28 per share. Morgan Stanley & Co. Incorporated acted as lead manager and Hambrecht & Quist LLC acted

as co-manager of the underwriting group. In one of the most stunning debuts in stock market history, the stock soared to a high of $74.75 before ending the day at $58.25. The stock continued to climb, reaching a price of more than $160, and in November 1995, Netscape announced that its board of directors had approved a two-for-one stock split.

65. Netscape launched offices in Paris, London, and Munich in 1995. We also entered the Japanese marketplace with a Tokyo-based wholly owned subsidiary, Netscape Communications (Japan) Ltd., and established relationships with nine leading Japanese resellers.

66. By the end of 1995, Netscape had an over 70 percent market share for Internet clients and had distributed 15 million browsers around the world through a variety of channels including ISPs, OEMs, and resellers as well as over the Internet.

67. Also by the end of 1995, @Home had licensed Netscape's client and server software to be used as the foundation for the @Home network, a high-speed broadband network providing Internet access to personal computers via cable. More than 12,000 developers had joined our Netscape Development Partners Program. We counted 70 percent of the global Fortune 100 companies among our customers, including AT&T, Hewlett-Packard, Lockheed Martin, MCI, and Motorola. Our products were selected by large customers such as Dataquest, Discovery Channel Online, Dow Jones

Corporation, and MCI, who used Netscape Internet Applications as the basis for electronic commerce applications. In the technology realm, Netscape continued to innovate and to be a leader of the Internet industry.

68. In December 1995, Netscape and Sun announced JavaScript, an easy-to-use scripting language designed for creating live online applications that link together objects and resources on both clients and servers. As noted above, JavaScript later became an Internet standard under the name ECMAScript.

THE MICROSOFT MONOPOLY IS THREATENED BY THE INTERNET

69. In order to understand the threat that the Internet posed to Microsoft's operating system monopoly, some brief background regarding the relationship between operating systems, applications and the Internet is necessary. While the computer's operating system does not perform the functionality that applications do, it is critical to the proper functioning of those applications. An operating system is the "central nervous system" of a personal computer. It controls the interaction between the computer's processing unit or chip, memory, and attached devices called "peripherals," such as keyboards, disk drives, display monitors, and printers. In addition, the operating system serves as a "platform" from which applications, such as word processing, spreadsheet, financial accounting, browsers, and games can be launched.

70. The operating system is able to serve as a platform because it provides

"system services" that other software developers can use when writing their own software programs. These system services are available through features in the operating system known as application programming interfaces ("APIs"). For example, when a computer user wants to print a word processing document, the word processing software program issues a "call" to a particular API. The operating system will then essentially "instruct" the computer to perform the function associated with the API by causing the microprocessor to carry out the instructions. That same API can be used by any number of programs. For example, the same API that causes a word processing document to be printed can also be used by a programmer writing software for financial accounting or spreadsheets and cause documents created in those applications to be printed.

71. APIs are critically important to software developers. Software developers are the computer programmers who write the variety of applications that run on operating systems. It is those applications that enable computer users to perform the functions they want from their computers. Although Microsoft clearly has the monopoly on personal computer operating systems, there are other operating systems. In addition to Microsoft's several operating systems -- Windows 98, Windows 95, Windows 3.1, and Microsoft Disk Operating System ("MS-DOS") -- there has been over time and continues to exist in the installed base other operating systems with very small market shares, such

as IBM's OS/2 system or Apple's Macintosh system. All of these operating systems have unique APIs. This means that software applications written for one operating system will not run well on any other operating system. For example, software developed and programs written in code for the Windows platform will not run (or at least not run properly) on the Macintosh platform or the OS/2 platform. The fact that applications must be written to specific operating systems is commonly referred to as making the applications "platform dependent," because the ability to run the application, and therefore the utility to the computer user, depends entirely on the underlying operating system. Thus, computer software developers will generally write software that runs on the most ubiquitous operating system. Because of the dominance of Windows, the practical effect is that the vast majority of personal computer applications written today are written to the Windows operating system platform.

72. This technological lock-in has enabled Microsoft to achieve and reinforce its monopoly position in personal computer operating systems. To understand why this is so, it is important to understand that consumers expect that the computers they purchase will be ready to use. That means that, when a consumer brings a personal computer home and opens the box, he or she expects to plug it in, turn it on, and start to work or play. Thus, OEMs ship computers with preinstalled operating systems and a variety of applications

that are chosen by the OEM to add value to the OEM's computer offerings. Today, well over 90% of the personal computers sold in the world have a Microsoft operating system preinstalled by the OEM. This substantial "installed base" leads to some very predictable results, all inuring to Microsoft's benefit.

73. Independent software vendors, or "ISVs" -- those people who develop and distribute applications software that consumers buy -- understand the reality of the marketplace and recognize that well over 90% of personal computers sold in the world today come with a Microsoft operating system preinstalled. Since applications are platform dependent, ISVs looking at this world quite sensibly write most of their software for the platform with the widest use. That means that most applications are written for the Windows platform.

74. The fact that most of the software applications are written for the Windows platform only reinforces Microsoft's monopoly position in operating systems. Because so much software is written for the Windows platform, consumers who want to take full advantage of their computers and to have the maximum number of choices of applications available continue to purchase machines with a preinstalled Windows operating system. At the same time, the more personal computers sold with Windows operating systems, the more ISVs continue to write applications for the Windows platform. In other words, the sale of computers with Windows operating systems feeds the

development of software for the Windows platform, which in turn, generates additional sales of computers with Windows operating systems. To its credit, Microsoft's early recognition of this type of network effect allowed it to achieve a monopoly in operating systems.

75. ISVs could, of course, write the same applications programs to work on other operating systems, a process referred to in the computer industry as "porting." It is time-consuming and expensive, however, to take a piece of applications software developed for the Windows platform and port it to the OS/2 or Macintosh platform or to some other platform. Moreover, because the market for a product successfully ported to a non-Windows operating system is smaller, there is no guarantee that an ISV can recoup the investment made in porting an application from the Windows platform to another platform. Thus, ISVs have very little economic incentive to spend the resources to port to non-Windows platforms. Again, this further contributes to the dominant and almost impregnable market position Microsoft has obtained in personal computer operating systems.

76. When Netscape entered the "Windows World" as we found it in late 1994 and early 1995, we knew our "window of opportunity" was building the bridge between the platform dependent computer operating system world and the cross-platform environment of the Internet. In fact, we realized that we needed to build an Internet browser that would run not only on all different

personal computer operating systems, but also on non-personal operating systems (UNIX, etc.). Netscape was founded on the principle of making the tremendous amounts of information on the Internet available in an easy-to-use format to the entire market; thus, Netscape founders did not want to arbitrarily exclude UNIX or OS/2 users from the community of people who would be able to reap the benefits of the Internet and the Web. The Netscape engineers came out of an academic environment that favored UNIX, Mac, and OS/2 over Windows. We believed it was important to provide the same level of accessibility to the Internet to people working in these environments as well as to those working with Windows. Thus, the universal nature of the Internet and the commitment to open standards by Netscape and its founders demanded the creation of a cross-platform browser.

77. The development of Internet browser technology, particularly Netscape's Navigator, and the influence it had on the widespread consumer use and acceptance of the Internet provided an opportunity to level a playing field that had been heavily tilted by Microsoft. The Internet is a global network of various individual computer networks linked together. Indeed, its name "Internet" is short for "interlinked networks," and, as commonly used today, refers to separate computer networks that are capable of communicating with one another. The World Wide Web, discussed below, is a portion of the Internet.

78. The Internet's origins date back to the 1970s, when military personnel attempted to ensure that various computer systems in the United States would not be significantly disrupted if a single computer or single connection between two or more computers was destroyed. Rather than establishing a single computer network in which a central computer or computer facility manages the network, the Internet was created as a network of networks.

79. This multiple network structure could function, however, only if the many networks were able to exchange data with one another regardless of the type of computers used by any individual network. To solve this problem, the Internet uses an open standard, known as Transport Control Protocol and Internet Protocol ("TCP/IP"), that enables different computers to communicate with one another. This network of networks got a further boost from the development of hypertext, which allows a computer user to move from one page to another page (also in hypertext) by clicking on highlighted text in the original page. In 1989, researchers adapted hypertext to the Internet by developing Hypertext Markup Language ("HTML") and Hypertext Transport Protocol ("HTTP"). HTML enables one hypertext page to be linked to another anywhere on the Internet, and HTTP manages the transmission of HTML pages. The universe of HTML documents linked together on a network using TCP/IP is what we know as the World Wide Web ("Web").

80. These computing advances allowed previously closed and isolated computer networks to communicate and exchange data with one another. Theoretically, anyone with a computer could link to this network, but the one missing feature of the Internet was software that allowed average computer users to move or navigate easily through the maze of interlinked computers, to find and access particular HTML pages, and to display them on their computer screens. Netscape helped fill that gap with the development and commercial release of its Internet browser, the Navigator. With the release of the Navigator, the Internet became instantly and widely accessible to the public at large, regardless of which operating system a particular consumer's computer ran. The public responded enthusiastically. From an enterprise (or commercial or organizational customer) perspective, Netscape also generated great enthusiasm because in addition to providing this mechanism to navigate the Web, Netscape ported Navigator to many different platforms, including UNIX, Mac OS, and OS/2. Thus, by adopting and employing Navigator as their Internet browsing software, enterprises could provide their employees with a consistent way to browse the Web or their internal network, regardless of the operating system on a particular user's machine.

81. As stated previously, the initial launch of Navigator in 1994-95 was very successful. By the end of our first year, it was quite clear that Netscape was at the forefront of an emerging and increasingly popular technology

revolution. Microsoft was late in recognizing the commercial potential of the Internet and the implications that it held for personal computing, but there is very little doubt that development of the Internet and the Web and its accessibility to the large mass of the consuming public, which was made possible in large part by the development of Netscape's browser, posed a serious threat to the Windows operating system monopoly.

82. Netscape's browser, like other software, runs on top of a personal computer operating system. But unlike the typical application, the Netscape browser not only provides a graphical user interface for computer users, but also is a platform from which applications are launched. I am not suggesting that the browser is a replacement for the operating system; Navigator still needs an operating system, such as Windows 98, running underneath it, but Navigator can and does serve as a platform for certain network-centric applications.

83. The development of browser technology opened up a number of important possibilities in the computer industry. While Netscape was developing and commercializing an Internet browser, Sun Microsystems was developing Java, a programming technology. The Java programming technology solves the platform dependency problem that has so long plagued software development. Programs written in Java can be run on any platform that has a Java virtual machine and Java class libraries, which Navigator does.

84. Because Netscape's browser made access to the Internet and the World Wide

Web widely available to the public, it gave ISVs reason to begin writing a number of programs in the Java language, as well as other OS-neutral languages. It also gave ISVs a number of options for how to configure their software. Prior to the development of the Netscape Navigator, most applications software resided on the hard disk of a personal computer. The Windows operating system essentially managed software applications residing on that specific computer. The development of the Navigator, however, gave ISVs the opportunity to distribute their application code in any fashion they chose. For example, all of it could be on the specific computer used by a computer user (known as the "client"), or all of it could be on a centralized computer (known as the "server") that serves a number of personal computers, or some code could be on the server and some on the client. There are other options available as well. For example, software applications could be accessed from the Internet. This flexibility expanded the capability of applications software and made possible new categories of applications.

85. These innovations arising from the development of browser technology, particularly Navigator, were eventually noticed at Microsoft. The possibility of a vast library of applications written in Java or other OS-neutral languages coupled with independent user interfaces and platforms, such as those provided by Navigator, posed a serious threat to the Windows

monopoly. If ISVs began writing a number of programs in such languages, computer users with a browser could launch those programs from the browser platform without regard to the underlying operating system. In other words, it would not matter to the consumer whether the computer had a Windows operating system, Macintosh, OS/2, UNIX, or any other operating system. The rise of the Internet and browser technology, coupled with Java and other new languages, promised the development of "platform independent" software. ISVs would be able to write a program once, and it would run on any computer.

86. At the time I joined Netscape in early 1995, to my knowledge Microsoft had not begun to capitalize on the development of the Internet and the Web. By May 1995, however, as I have learned, Microsoft did recognize the significant threat that the Internet and browsing technology posed to its operating system monopoly.

87. In short, the rise of the Internet, which was heavily promoted by Netscape, the development and commercial success of browser technology in general and Navigator in particular, and the development of Java made possible the day when the specific operating system on a particular computer would no longer be a constraint on the type of software that computer could run. ISVs could avoid expensive "porting" costs and write applications in Java, knowing that they would run on any computer. Computer manufacturers would still

preinstall operating systems, but they would be free to choose the system, be it Windows, OS/2, Macintosh, or some other operating system, that provided optimal performance at the lowest possible cost.

88. These innovations, however, suffered a significant setback because Microsoft engaged in a variety of business practices designed to stifle these developments and to co-opt or crush anyone, including Netscape, that had the temerity to compete with it. The purpose and effect of Microsoft's conduct was to maintain the monopoly position of the Windows operating system.

89. **Browsers Are Applications** – Before I move to the specific actions Microsoft took against Netscape to try to protect and expand Microsoft's monopoly, I think it is important to make one point clear: a browser is a separate product -- an application, essentially like the spreadsheet programs and word processing programs discussed above. While this point seems so clear to me that it should not warrant separate discussion, I have seen it reported that Microsoft claims that its browser product is simply an upgrade to its operating system. Therefore, I must address this issue.

90. Netscape Navigator and Netscape Communicator are indisputably applications or products separate from the operating system; they can not run without an operating system, such as Window 98. Consumers have had no problem appreciating that browsers are separate products. Although our market share has been decreasing, consumers still demand Netscape

Navigator and Netscape Communicator separately from any operating system products. Indeed, Netscape does not sell any operating system products, and was able to sell millions of browser licenses to consumers and enterprises separately from any operating system. Moreover, the industry as a whole recognizes browsers as separate products from operating systems. Browser market share is tracked (separately from operating system market share) by many third party organizations, such as IDC and DataQuest. The "browser wars," referring to the commercial battle between Netscape Navigator and Microsoft Internet Explorer, are frequently reported on in the press. I have seen many product reviews comparing Navigator to Internet Explorer; I have never seen a product review comparing Navigator to any Windows operating system.

91. Significantly, Microsoft also has treated browsers as a separate application from the operating system. To compete with Netscape, Microsoft began offering cross-platform versions of Internet Explorer. These cross-platform versions are separate products from Windows or from any operating system. Indeed, Microsoft still offers a downloadable, stand-alone version of Internet Explorer on the Web, and Microsoft actively promotes its "download Internet Explorer" program. If you look on almost any major web site, you will see a "download Internet Explorer" button -- not a download an "Upgrade to Windows" button. Microsoft also has participated in the "browser wars,"

reporting Internet Explorer's market share on a regular basis, and comparing the features of Internet Explorer to Netscape Navigator or Communicator -- not to any operating system.

MICROSOFT RESPONDS TO THE THREAT

92. Once it realized the threat the Internet and browsing technology posed to its operating system, Microsoft began an unrelenting, and in my view illegal, campaign to protect its monopoly. Microsoft's response to the competition by Netscape was two-fold: first, an attempt to divide the market and, when that failed, a campaign to eliminate Netscape as a viable browser company by systematically shutting down our distribution channels and by engaging in other predatory acts.

93. With regard to Microsoft's effort to divide the market with Netscape, it is important to provide a brief background of the relationship between the two companies. Netscape builds products that run on Microsoft's operating system. Like any independent software vendor, ("ISV"), we are engaged, even today, in ongoing communication with Microsoft and other operating system vendors to be sure our software functions properly with the operating system. We have both formal and informal contact, the latter often occurring at industry conferences. I had one such conversation at a Hambrecht & Quist Entertainment Conference at Snowbird with Dan Rosen who was then Director of Strategic Relations of Microsoft. I knew Dan prior to this meeting

at Snowbird because he and I had worked at AT&T, after the AT&T acquisition of McCaw Communications. The conversation Dan and I had at Snowbird was very casual and friendly. He explained to me that he was the Microsoft person responsible for forming strategic relationships regarding the Internet and communications technologies. Dan described to me the nature of some of the sorts of deals he had been working on at Microsoft. Based on our conversation, I believed future discussions might be fruitful. Dan and I agreed to continue our discussions at a later date. I believed my prior relationship with Dan and his position with Microsoft presented an opportunity to build some sort of productive relationship between the companies. I was definitely interested in having Microsoft as an ally, not as an enemy, and hoped this discussion was a step in the right direction.

94. After this first conversation with Dan, I believe I had a couple of telephone conversations with him. At the time, I was aware that others at Netscape were talking with Microsoft about the adoption of a security protocol that Netscape had developed, called SSL, and a security protocol that Microsoft was in the process of developing, called STT. As I recall, these discussions were not proceeding very quickly. I vaguely recall that Dan initiated conversations to help move along the security protocol discussions.

95. I have reviewed certain e-mails sent by Netscape management and members of our engineering team prior to a June 2, 1995 meeting I had at Microsoft,

regarding Netscape's efforts to develop a browser that would work well with the upcoming release of Windows 95. At least as early as March 19, 1995, John Mittlehauser, a member of our technical staff and one of our initial hires, was corresponding with Thomas Reardon, Microsoft's Technical Lead of the Windows 95 Networking Group, about Netscape's work on a Windows 95 browser. (MS98 0135438). On April 11, 1995, Marc Andreessen, one of Netscape's founders and the company's Chief Technology Officer, corresponded again with Thomas Reardon about Netscape's Windows 95 plan. (NET 000957-58). On May 31, 1995, Tom Paquin, Director of Netscape Client Products, summarized several telephone conversations he had with Mr. Reardon, including specific discussions about technologies that would or would not be part of Netscape's Windows 95 browser. (NET 000199-000203).

96. I am also aware that there had been some discussions between Netscape and Microsoft prior to the time that I joined Netscape. I believe that Jim Clark, then CEO of Netscape, Ram Shriram, Netscape's Manager of OEM Sales, and Mike Homer, Netscape's Vice President of Marketing, had talked to Dan Rosen and others at Microsoft in the fall of 1994. I am informed that those discussions related, at least in part, to Microsoft purchasing or licensing Netscape's Navigator code. I am aware that those discussions did not prove fruitful because Netscape was not interested in Microsoft's proposal, which

was to purchase the Navigator code for what Netscape considered to be a low flat fee payment.

97. I have also very recently learned that in late December of 1994, Jim Clark sent an e-mail to Dan Rosen and Brad Silverberg, Microsoft's Senior Vice President, Personnel Systems Division, attempting to renew efforts to discuss the possibility of Microsoft licensing the Navigator code, even though Netscape was aware that Microsoft had by then already licensed the Spyglass browser code. Jim Clark has described this as a moment of weakness. In December of 1994, unsure of how to direct Netscape's business after having invested a substantial amount of time and money in the company, Clark was already searching for someone to replace him as CEO of Netscape. Indeed, Clark and John Doerr, one of Netscape's principal financial backers, had contacted me in mid-1994 about being CEO. I had accepted a position on Netscape's Board of Directors in October to consider the possibility. I have also recently learned that Jim's e-mail stated his opinion that there was no money to be made in the browser market. Jim did not tell me or the Board of Directors about this e-mail, and his opinion proved to be wrong. Netscape had just released its first commercial version of the product on December 15, 1994, and by the end of the first quarter of 1995, Netscape already had earned over $2 million in revenues from the browser alone. Although Jim expressed this opinion in late December of 1994, I already was developing a

contrary opinion. As the history of Netscape's browser revenue in 1995 alone demonstrates, I came to believe that significant revenue could indeed be generated from browser licensing. My opinion proved to be correct. Over one half of Netscape's 1995 revenues of approximately $85 million dollars was earned through browser licensing.

98. In May of 1995, Dan Rosen raised directly with me the issue of some sort of strategic relationship between our companies. Dan raised that issue at a time when we were spending tremendous resources on developing a Windows 95 version of Netscape Navigator. Windows 95 was scheduled for release in mid-summer, and we planned on releasing a compatible browser simultaneously. However, we were having difficulty getting the necessary technical specifications and licenses from Microsoft. I agreed to speak further with Dan in order to resolve these issues and to try to build a working relationship with Microsoft, as we discussed at Snowbird.

99. During mid-May, 1995, Dan and I set up a formal meeting to discuss these issues. The issue of forming a relationship with Microsoft was discussed at length among the members of the Netscape executive staff during May. For what turned out to be good reason, a few members of my executive staff expressed concerns about being too open with Microsoft. Microsoft already had publicized its intentions to develop a competing browser, and thus some members of the executive staff were hesitant to disclose all the newly planned

features of the browser, particularly because, at this point, Netscape was counting on browser revenue to be a significant portion of its total revenue. Netscape's browser revenue more than tripled from the first quarter of 1995 to the second quarter of 1995. We did not want, and could not afford, to compromise that revenue.

100. Despite those reservations, I agreed to meet Dan on June 2, 1995. Prior to the meeting we had some substantive discussions about Netscape's plans. In addition, I was aware that other people within Netscape were still trying to obtain the necessary technical information from Microsoft to design a retail version of Navigator that would work well with the upcoming Windows 95 release. At this point, the Navigator version for Windows 95 already had been released in a pre-commercial or beta form on the Web.

101. On June 2, 1995, I met with Dan, Nathan Myrhvold, Microsoft's Senior Vice President, Virtual World Group, and Paul Maritz, Microsoft's Senior Vice President, Consumer Systems Division. The meeting was cordial and explored possible areas of collaboration between the two companies. I recall that Microsoft principally was interested in getting me to consider adopting certain security protocols, incorporating into Navigator certain viewers that would enhance Microsoft content, and other technologies related to our browser. I also recall that Microsoft stressed some server issues, including the potential of packaging a Netscape server product with Microsoft NT. I

also recall focusing on our browser product. I told Dan, Paul, and Nathan that we were gearing up for a retail release of Navigator and that we were already quite happy with the revenue we were generating from browser licensing. At one point during the meeting I suggested that Microsoft distribute Netscape's browser, often referred to as "the client." Although I did not think that Microsoft would take me up on this offer, I wanted to stress the importance of the client to Netscape's business strategy. I also recall that Marc Andreessen had asked me to raise several issues related to both browser and server technology. I recall that Microsoft was receptive to Marc's ideas. I also told Microsoft that continuing to improve the client was consuming a large portion of Netscape's engineering resources at that time. Finally, I recall discussing the importance of enterprise software to Netscape. The meeting ended in a friendly fashion, and we agreed to meet again.

102. I drafted some brief notes of the June 2 meeting and circulated them to my executive staff. As was my practice, the notes focused primarily on what Microsoft communicated to me. I have recently reviewed my notes and to the best of my knowledge they accurately reflect what Microsoft communicated to me during the June 2, 1995 meeting. (NSMS 60813).

103. About a week after the meeting, Dan Rosen forwarded his notes of the meeting to me at my request. I read his notes and agreed that they generally comported with my recollection of the meeting in terms of possible areas of

collaboration. I have recently reviewed Dan's notes (NET 00209-12) and agree that they accurately represent a portion of the discussions at the June 2 meeting. In particular, the notes confirm my recollection that I told Dan, Nathan, and Paul that Netscape's direction included "selling lots of site licenses for browsers," and that Netscape would only waive the license fee for students and non-profit organizations. Moreover, the notes confirm that I informed Microsoft of Netscape's planned retail launch of Navigator. The notes also confirm that I told Dan, Nathan and Paul that Netscape's browser plans focused on the Windows platform. Finally, I informed them that I believed that Netscape's primary competitor was Lotus Notes, and not Microsoft. That was an accurate statement at the time, because Microsoft had not yet announced its intention to displace Netscape from the marketplace by creating its own browser, bundling it with the operating system, and shutting us out of numerous browser distribution channels.

104. In sum, at the June 2, 1995, meeting I clearly communicated to Microsoft that Netscape was investing great resources in developing its browser, particularly for the Windows 95 platform, that Netscape planned a retail release of the browser, and that Netscape intended to earn money from browser revenues. Indeed, much of the technology that Microsoft was advocating that Netscape adopt, in particular the viewers, related to the Netscape client.

105. After the June 2, 1995 meeting, Dan and I had several additional phone calls. The primary purpose of the phone calls was to set up a meeting with a larger group of people from both Netscape and Microsoft. The plan was that Microsoft would do presentations on the technologies they were interested in having Netscape adopt, followed by question and answer, and a further discussion of both parties' plans. Dan circulated a draft list of items to be discussed at the meeting (NET 000017-19). Marc Andreessen sent an amended list of discussion items back to Microsoft. (NSMS 51545) The amended list indicated items that we thought were most important. Our top priority was to obtain APIs and other technical information we needed from Microsoft in order to release a browser compatible with the Windows 95 operating system. As discussed below, I had been informed that we had been having difficulty getting timely and helpful responses from Microsoft personnel on these issues. We hoped that the meeting would solve these problems. The meeting was set for June 21, 1995 at Netscape.

106. **The June 21, 1995 Meeting – Microsoft Proposes Dividing The Market** – As discussed above, we needed certain technical data for our browser to be ready for release with Windows 95. For example, we needed the Remote Network Access ("RNA") phonebook API from Microsoft. We also needed other technical information from Microsoft, including a scripting engine in beta, and the most recent version of Windows 95. We needed to get

this data from Microsoft quickly, in order to release our retail browser product at about the same time that Microsoft launched Windows 95. We still had not received that technical information when several Microsoft employees came to our offices for a meeting on June 21, 1995.

107. Mike Homer, Andreessen, and I represented Netscape at the June 21 meeting. Rosen led the Microsoft contingent, although he was accompanied by a number of other Microsoft employees, only some of whom I remember. Marc Andreessen's notes of the meeting indicate that the other Microsoft attendees were Anthony Bay, J. Allard, Tom Reardon, Chris Jones, Barb Fox, and Richard Wolf. I remember that, for the most part, each Microsoft employee appeared to be responsible for discussing a different area of technology.

108. The discussion at the meeting covered some of the matters on which Andreessen and Rosen had previously communicated. Microsoft personnel made presentations about the various technologies that Microsoft was interested in persuading us to adopt. Mike Homer and I asked questions. Andreessen, for the most part, typed notes of the meeting on his notebook computer. Marc, who is an extraordinarily fast typist, frequently typed notes during meetings, and, on this particular occasion, I may even have asked him to take notes.

109. The technology discussions were largely unremarkable, in my recollection. I

believe there was a presentation on a security protocol Microsoft was advocating and on some Microsoft Office related technologies. I do not have any other recollection of the technology presentations.

110. The most notable thing about the meeting was something entirely different and something not covered in the proposed agenda. Microsoft's officials made it clear that they believed that Netscape should work with them on areas other than a browser for Windows 95, but that we should not develop our own browser for Windows 95 because they intended to build a Microsoft browser for the Windows 95 operating system. They proposed that a "line" be drawn between the area in which we developed products and competed and the area in which they developed products. Microsoft proposed that we build products that would run on top of the Windows 95 operating system and browser. They offered to allow us to continue to develop browsers for other operating systems, as long as we did not try to compete with them in developing a browser for the Windows 95 platform, which, of course, we all anticipated would shortly be the dominant operating system. Microsoft also proposed making an investment in our company and obtaining a board seat. Microsoft officials said that, if we agreed to the "special relationship" they proposed, Microsoft would support us by making Netscape a "preferred" ISV. The Microsoft personnel made clear that issues concerning the RNA API and related technical information we had been seeking could be resolved

"[d]epending on how we walk out of this room today." If we agreed to the "special relationship" that they proposed, the Microsoft representatives said that we would be the first ISV to receive the technical information, mentioning that they already had an internal solution for the issue we were addressing.

111. Recognizing that our main goal for this meeting was to get access to certain code and APIs necessary for our product development, I remember asking whether obtaining those things was tied to our acceptance of this "special relationship" Microsoft had proposed, including the market division, equity investment and board seat they proposed. Microsoft's answer was that our obtaining the necessary technical information "certainly isn't independent" of our accepting their proposal. This fairly clear threat bothered me greatly. If we refused to agree, Microsoft made it very clear that they would attempt to crush us by attempting to own the client.

112. I have never been in a meeting in my 33-year business career in which a competitor had so blatantly implied that we should either stop competing with it or the competitor would kill us. In all my years in business, I have never heard nor experienced such an explicit proposal to divide markets. Soon after the June 21 meeting, I reviewed Andreeseen's notes. (NET 000230-36). I did not send Marc any corrections, as would have been my practice if I had any concerns, because I believed the notes to be accurate at

the time I read them. I have reviewed them again recently. While I do not have a precise current recollection of all the details of the meeting, I do not disagree with anything in Andreessen's notes, which reflect the following assertions by Microsoft personnel:

a. Microsoft made clear that the "set of things that are provided in Internet servers and browsers" would be "in the core operating systems or given away with the OSs as a facility like the Win32 API." What Microsoft wanted was "a partner" who would "take those core services to build on top of them and create solutions for customers." Microsoft wanted to know whether Netscape was "the kind of company that's going to partner with MS on this or not."

b. Microsoft informed us that if we did not have a "tighter relationship" with it, Netscape would be "back to what a normal ISV can do." On the other hand, if we agreed to "a tight relationship," then Netscape could get "tight integration."

c. Microsoft's representatives asked us whether Netscape would "be interested in a partnership where NS gets all the non-Win95 stuff and MS gets all the Win95 stuff." If we did not agree, "then that's one thing. If NS does want to, then we can have our special relationship." As Andreessen's notes make clear, we understood that to be a clear threat that "MS WILL OWN THE WIN95 CLIENT MARKET AND

THAT NETSCAPE SHOULD STAY AWAY."

d. When we asked about the RNA API and other technical information we needed, Microsoft's representative said that "[w]e can fix that problem." Microsoft admitted that there was "internal stuff that implements internal APIs, and those APIs are only known inside Microsoft." We were told that "[d]epending on how we walk out of this room today, we have a solution for your problem." We were told that "[i]f we had a special relationship, you [Netscape] wouldn't be in this position." If we did not agree to their proposal, we were told that we could not expect the APIs and other technical information for three months.

e. When I asked whether receipt of the APIs and other technical information was related to their proposal to divide markets and to make an equity investment in Netscape, the response from Microsoft was the "[i]t certainly isn't independent."

113. We rejected both Microsoft's offer to divide markets and the remainder of their proposals. Most of the matters on which they would have had Netscape confine its work were not commercially valuable. Essentially, Microsoft was offering to allow us to work with them on matters that did not amount to much and would not have been particularly important to Netscape. In exchange, Microsoft would have obtained an equity stake in Netscape, a

board seat, and our agreement not to compete with them in the Windows 95 browser market. We simply would not and could not agree to those things.

114. Interestingly, we did not receive the APIs and other technical information we had been seeking until October 1995 -- or approximately three months later, which was well after the launch of Windows 95 and was precisely what Microsoft had threatened at the June 21 meeting.

MICROSOFT'S PREDATORY PRACTICES AFTER THE JUNE 21, 1995 MEETING

115. After Netscape refused Microsoft's offer to divide the browser market, I began hearing reports that Microsoft was directly interfering with Netscape's ability to license and distribute its browser software. Microsoft's interference took many forms. I will detail below some of the many reports I received concerning these matters. However, before setting out the details, I will summarize the general pattern of Microsoft's behavior, Microsoft's own statements that corroborated the reports I was receiving, forwarded documents that we received that originated from Microsoft and corroborated the reports I was receiving, and press accounts I was aware of that corroborated these reports. It must be stressed that Microsoft's comments to the press alone were significant. Specifically, Microsoft's comments about Netscape appeared designed to create doubts about Netscape's ability to compete in the market. Given the power that Microsoft, and in particular,

Mr. Gates, has in influencing the computer industry and analysts, Microsoft's negative comments, as intended, directly affected Netscape's ability to compete effectively. It was not a totally uncommon event for a customer to question whether it made sense to do business with Netscape because of Microsoft's public position that it was going to crush Netscape's business.

116. Indeed, neither Bill Gates nor other Microsoft executives were shy about describing publicly the threat they felt Netscape posed to Microsoft and their intention to eliminate Netscape as a competitor. I became aware of numerous press and other statements from Microsoft executives, including Mr. Gates, in which Microsoft expressly manifested its intent to crush Netscape.

117. On the anniversary of Pearl Harbor Day, December 7, 1995, Microsoft detailed its Internet strategy in a day-long session for press and analysts. During the briefing, Bill Gates announced that Microsoft was "hard-core about the Internet." His company's public plans for storming the market included giving away for free all versions of Internet Explorer (which, of course, competed with Netscape's browser), including versions that ran on non-Microsoft operating systems, and Microsoft's web server (which competed with a Netscape server), and then including them in the Windows operating system and the Windows NT operating system. The Seattle Times, in a front-page article entitled "Microsoft plays Hardball" and subtitled "Game Plan for

Internet: Crush the Competition," reported that during the briefing Microsoft executives Greg Maffei and Paul Maritz gloated over the $30 drop in Netscape's stock price that resulted from the Gates announcement, and reported that another of their colleagues said of the precipitous drop in the stock price, "That's not enough." The Seattle Times also reported that, given the 100 million customers of Windows and Windows NT, distribution would be extremely important for Netscape; it quoted one analyst present at the event as saying that Netscape "had better react quickly to find mass distribution for its own Internet-browsing software."

118. In March, 1996, in response to the combined threat of Java and Navigator, Microsoft attempted to turn the Internet from an open system to a Microsoft proprietary system. For example, ActiveX was Microsoft's effort to make developers create software and content which bound the Internet to Windows and played a key role in Microsoft's "Embrace and Extend" strategy. ActiveX was introduced with great fanfare at Microsoft's first Internet developer conference in March 1996. Microsoft promoted ActiveX as the primary way in which websites should be built.

119. In June of 1996, Bill Gates told the Financial Times of London, that:

> 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. (Financial Times of London, June 16, 1996, at 15.)

120. Mr. Gates again made negative comments about Netscape in July of 1996.

Infoworld reported on July 29 that Bill Gates snapped at reporters asking him about developers adopting Netscape APIs. According to the article, Gates made a point to:

> position Netscape as a middleware company. He then reminded the assembled press that historically, middleware companies do not last long. Any lead Netscape has, Microsoft hopes to erase or to quote [Gates] 'what part of the fact that Microsoft owns Windows don't you understand?'" (NSC 002005-002006)

121. On August 9, 1996, Microsoft held a briefing for various venture capitalists ("VCs"). Paul Maritz, John Ludwig, Skip Madigan, and Greg Maffei were the Microsoft executives in attendance. Their main points, as reported to me, were that Windows NT and Windows 95 had won in the marketplace, and that Microsoft was shipping Internet Explorer 3.0 with every Win 95 desktop from Q4 1996 forward. They indicated that this strategy would drive leadership for Internet Explorer and Active X against Navigator and Java. They also stated that Microsoft supports Java the programming language, but is directly opposed to Java the OS. I was told that Microsoft indicated that with a client competitive with Netscape's and Internet Explorer bundled into every Win 95 desktop from Q4 1996 on, Microsoft ultimately will win the client war (resulting in 3-4 million more browser seats for Internet Explorer every month). It was pointed out to me that Netscape's brand and user loyalty would be mitigated by Internet Explorer being made part of the Win 95 desktop by Q1-Q2 1997. By winning the client war, Microsoft would

secure dominance for Active X and marginalize Java. (NSC 71544-71545).

122. Although Microsoft now conveniently attempts to blame Netscape's decline in market share on our allegedly bad decisions or management, Microsoft did not always harbor that opinion. In addition to stating over and over again that it intended to crush Netscape, Microsoft on a few occasions admitted the reasons for its fears. Steve Ballmer stated in September of 1996: "Have no confusion in your head: Job one for us right now is the Internet and defeating Netscape . . . ***[Netscape is] simply our smartest competitor.***" ("Microsoft - On Top for Now - As it Wages War on all Comers, Maintain its Dominant Position?" VAR Business, 9/5/96) (emphasis added).

123. Apparently facing a worthy adversary, Microsoft could not resort to competition in the open marketplace, but rather resorted to using its monopoly to ensure a win. Starting soon after our rejection of Microsoft's June 21, 1995 proposal to divide the browser market, Netscape began hearing numerous reports of Microsoft practices designed to use its monopoly power in the operating system to prevent us from competing in the browser market. These reports are detailed below, based both on my recollection and on my review of Netscape e-mails. Because the pattern had become so pervasive, at some point in time we began keeping track of reports of Microsoft's actions, and thus I am able to recount detail about those instances from our company records.

124. These Microsoft practices included exclusionary contracts that prevent customers from choosing to deal with Netscape, and other efforts to restrict Netscape's access to the channels of browser distribution, such as ISPs, OEMs, ISVs, ICPs and Corporate Accounts. In addition to restrictive contracts, these efforts included not only giving away the browser for free, but also offering compensation that amounted to making it "better than free" in many circumstances. That is, through cash or products or services, Microsoft was paying companies to replace Navigator with Internet Explorer. As set forth below, Microsoft engaged in other predatory acts designed to eliminate Netscape as a competitor, including building into the operating system unnecessary technical incompatibilities with Navigator's browser; and deliberate and critical delay in providing to Netscape technical licenses necessary for Netscape products to work properly with Windows. Examples of each of these types of predatory conduct are discussed below.

125. **Moves to Limit Netscape's Distribution Channels** -- There are several ways Netscape gets its Navigator browser, or client, to customers. These distribution channels include: distribution through ISPs, distribution through OEMs, distribution through ISVs, distribution through ICPs, direct sales to corporate users and consumers, and downloading via the Internet. For home users, the ISP and the OEM channels are by far the most important. Distribution in the other channels is not and cannot be a

substitute. The ISP and OEM channels statistically comprise the two largest distribution channels for all browsers, and those channels are especially important for new users. A user signs up with an ISP specifically for the purpose of getting connected to the Internet. If his or her ISP offers a browser, that user is highly likely to continue to use that browser. Likewise, many consumers purchase new computers just to get connected to the Internet. In this case, the new user is likely to use whatever browser comes already loaded on the computer. Even if a computer purchaser did not buy the computer specifically to connect to the Internet, that individual is likely to use the OEM-installed or bundled browser for the obvious reason that it is there. Adding an additional browser takes more work and, if the first browser can not be removed, uses additional computer memory, as well.

126. Microsoft engaged in many practices designed to interfere with Netscape's ability to distribute its browser in almost all of these channels. Primarily, Microsoft used its operating system monopoly to coerce exclusionary or restrictive contracts with ISPs, OEMs, ISVs, and ICPs. Microsoft also threatened to withhold access to its most precious asset, its operating system, and used its economic power to offer Internet Explorer for free -- and in many instances for better than free.

127. Evidence of these practices in each of the distribution channels is detailed below. In many instances, I was directly involved and personally experienced

Microsoft's use of its power. In other instances, I was informed of Microsoft's practices by my sales force in the normal course of business. In other instances, Netscape was informed of Microsoft's practices by the affected third parties. In yet others, I learned in the press of Microsoft's practices. The press accounts were consistent with what was being reported to me by my employees. It must be stressed and will be seen from the details below that from 1995 to today, I heard reports of Microsoft's interference with Netscape's ability to compete on an almost constant basis. This interference took a serious toll on Netscape.

128. ***ISP Foreclosure*** – Netscape realized the importance of the ISP distribution channel early in the game, and began signing up ISPs shortly after its first retail release of its browser. Many ISPs, large and small, eagerly embraced Netscape's browser and agreed to distribute it to their customers. In fact, Netscape had over 1000 ISP contracts for browser distribution in 1995 and early 1996. These contracts generally gave the ISP a license to distribute a Netscape browser and provided Netscape revenue from license royalties. Today, due to Microsoft's exclusionary and restrictive licenses, virtually none of our ISP contracts remain in effect as negotiated. Most of the contracts were terminated outright by the ISPs in connection with entering into distribution contracts with Microsoft, and of those that were not terminated, the ISP retains the right to distribute the Netscape browser but without

commitment to pay a royalty to Netscape.

129. Netscape still has many ISP agreements. However, because of Microsoft's exclusionary contracts, Netscape essentially has been unable to distribute its browser through the world's largest ISPs, including AOL, and the effectiveness of distributing the browser through other top ISPs has been severely limited. Although there are thousands of ISPs, over 75% of the world's Internet users access the Net from the 8 to 10 largest players in the industry. ("Consumer Choice in Web Browsers - One Year Later," NetAction, July 7, 1998; "Survey: ISP Deals Favoring IE," CNet, July 1998) I understand that Microsoft entered into exclusive, or restrictive deals with all these ISPs.

130. I understand that Microsoft's exclusionary deals require that as much as 75 to 80% of an ISP's overall browser distribution be Internet Explorer, which is effectively force-feeding Microsoft browsers to customers regardless of their preference. Moreover, I am informed that Microsoft's exclusionary contracts prohibit ISPs from distributing Navigator unless specifically requested by a customer.

131. Netscape has contracts with the Regional Bell Operating Companies ("RBOCs"); but they are not exclusive. Netscape contracts with Southwestern Bell, Pacific Bell, Bell Atlantic, Bell South, and Ameritech require that Netscape be the "default" browser. Three things about these contracts,

however, distinguish them from the Microsoft contracts. First, we only included these default provisions in response, and as a counter, to Microsoft's restrictive contracts, and these provisions sunset if and when Microsoft drops its exclusisionary requirement with AT&T and MCI. The pertinent language reads:

> Relationship to Other Browsers. For so long as AT&T and MCI (or any successor to MCI by merger) are both restricted by agreement from providing Navigator to their customers on a par with browsers of Navigator's primary competitor, Company agrees to the following:
>
> > Unless specifically requested otherwise by a customer, Dial-Up Kit will be the "default" browser for copies provided in physical media (i.e., floppy disk and CD-ROM) for Company's Internet Service on platforms for which Dial-Up Kit is available (such as Win95, Win 3.1 and MAC). Accordingly as to such platforms, although other client software (such as browsers) may be contained on the same media with which Dial Up Kit is made available, unless the customer has previously otherwise requested, Dial-Up Kit will be the default browser installation.
> >
> > Company will add the "Netscape Now" button to its web site on highly trafficked pages. Such pages will include links to an ftp location located either on the Company's web site or the Netscape web site, as selected by the Company. The placement and number of pages will not disadvantage Navigator on an overall basis as to links to other browsers.
> >
> > Browsers competitive to the Dial-Up Kit, and Company customizations to these browsers, may be available from Company web site, but in positions designed so as to not disadvantage Navigator itself on an overall basis.

> Once AT&T and MCI (or MCI's successor through merger) are no longer both restricted as provided above, Company, at its sole discretion, is free to continue all, any or none of the restrictions described in Section 15.1 without affecting any other provisions of this Amendment. (NSMS 004819)

132. Second, the Netscape contracts require only that the Netscape browser be set as the "default" browser. There is nothing in the contracts that prohibits the RBOCs from distributing another browser to their customers -- in any numbers. Third, the RBOCs account for less than 5% of the total ISP marketplace.

133. As is detailed below, Microsoft extracted exclusionary contracts from ISPs either by leveraging its monopoly power over the operating system desktop, or by using its economic power obtained through its monopoly profits to offer financial rewards to those that distributed the already free browser product.

134. The largest and most important ISP is AOL. In the fall of 1995, Netscape began negotiations with AOL to incorporate Netscape's browser into AOL's interface. This deal presented a very good distribution possibility for Netscape. Because of the obvious importance of securing distribution through the world's largest ISP, I personally invested a tremendous amount of energy in, and devoted a tremendous amount of Netscape resources to, closing the AOL deal. Netscape and AOL engaged in lengthy discussions about the technical feasibility of embedding the Netscape browser into the AOL system. After a lengthy technical feasibility study, both sides agreed

that the project was technically feasible and could be completed in an appropriate amount of time. One of the issues discussed in the technical feasibility study was AOL's desire for a componentized version of Netscape Navigator to use in its service offering. A componentized browser is essentially a browser that can be used inside another software program. Netscape had committed to componentizing its browser for AOL, and had committed to doing so on a schedule that met AOL's needs.

135. Microsoft was also negotiating with AOL toward the end of 1995. AOL told us that the reason they were negotiating with both companies was their desire to offer browser choice. Excited by the prospect of distribution through AOL, in March of 1996, after a long period of negotiations, Netscape entered into an agreement with AOL that did not provide for any exclusionary arrangement, but rather just a fair chance to let end users choose the browser they preferred. At the time of the agreement, both companies believed that Netscape could meet AOL's technical requirements.

136. The day after Netscape and AOL signed that agreement, AOL signed an ***exclusionary*** agreement with Microsoft that prohibited AOL from distributing the Netscape browser in any meaningful numbers. Of course, I knew why Microsoft was able to extract exclusionary terms from AOL -- its monopoly power over the desktop. Microsoft succeeded in getting exclusionary terms from AOL in exchange for space on the Windows 95

desktop, such that whenever users turn on their computers, they can access AOL right from the "first screen" or desktop. The fact that Netscape planned to charge for its browser and Microsoft did not, and that Microsoft already had a componentized browser and Netscape would develop one, came up in my discussions with AOL after they entered into the Microsoft deal. However, Steve Case and David Colburn of AOL confirmed my suspicions, both telling me that they would not have entered into the agreement with Microsoft but for access to the Windows desktop.

137. While there were some subsequent discussions between Netscape personnel and AOL about whether there was any other way Netscape could get its browser onto the AOL system, my understanding was that after AOL signed its exclusive deal with Microsoft, we were effectively shut out of this opportunity at least until that contract expired.

138. The exclusive deal with AOL cannot be brushed aside as a deal with just one ISP. Rather, AOL is by far the largest ISP in the country. Moreover, AOL's members account for over one third of Microsoft's Internet Explorer market share.

139. There are numerous other examples of Microsoft entering into exclusionary deals with ISPs. In March 1996, Netscape learned that after offering free software to an ISP, Microsoft added the following restrictions to the deal: "ISP cannot distribute any Netscape products. ... ISP cannot put anything

Netscape related on their [sic] server. ... ISP must put a 'viewed better with Internet Explorer' tag on their [sic] site." (NSC 001906) My understanding is that Microsoft entered into a variety of exclusionary deals with a number of the largest ISPs, including AT&T, MCI, and Earthlink/Sprint, PSI, NetCom, Compuserve, and MindSpring.

140. As an additional incentive for its exclusionary deals, Microsoft offered to give its browser to ISP's free or "better than free." In January of 1996, internal correspondence between Netscape's Peter Thorp and Ram Shriram, reveals that in negotiations with PSI, an ISP that was interested in licensing Navigator, PSI indicated that "Microsoft is offering to give them the world for free. They really want to do this deal and go with Netscape, but free [is] tough to argue with." (NSC 018811-018812).

141. Not only was Microsoft giving away its software, it was in many cases paying bounties to licensees whose customers signed up for Microsoft's internet services. A March 20, 1996, email from Fred Giordano, then Vice-President for Eastern Sales for Netscape, details a proposal Microsoft had made to Bell Atlantic. Under the proposed terms, Bell Atlantic would distribute Internet Explorer exclusively, would offer free Internet Explorer and Microsoft Network ("MSN") access to all its customers, and Microsoft would pay Bell Atlantic between $15 and $45 per sign-up. (NSC 001917)

142. On June 13, 1996 a Netscape sales representative from Northern Europe

reported that Microsoft offered free client product and a marketing fund of $400,000 to four major European ISP's (Planet Internet of Holland, Demon Internet of the UK, British Telecom of the UK, and Indigo/Dome of Ireland). "This was extended on the understanding that [they] would NOT purchase any [software] from Netscape." He adds that "there are a number of other examples which I could cite, however, these should indicate that we are seeing this type of predatory behavior in all countries with all major service providers." (NSC 001944-001945)

143. In September 1996, Netscape learned about the tactics Microsoft had been using to court Erol's, one of the largest ISPs in the East Coast of the U.S. According to Erol's CEO, Microsoft not only offered Internet Explorer for free, but also "offered to pay 20% of the $600,000 a month Erol's spends in advertising along with some other attractive incentives he didn't disclose." (NSC 002365)

144. In many cases, even when a potential customer preferred Netscape's technology, they felt forced to choose Internet Explorer because it was free. Danny Shader of Netscape described one such instance in a March 26, 1996 email: "As you know, Metro is establishing an on-line service called MetroNet that may/will be bundled with Vobis PCS. Apparently a manager at Metro named Peter Titz has expressed concern about the price we're asking for the Navigator bundle, and believes that if we don't soften, Vobis

will opt for MS Internet Explorer over Navigator. ... For technology reasons, our partner wants the deal to go Navigator." (NSC 018869)

145. A message forwarded to many Netscape employees shows how Microsoft was soliciting ISPs to switch to Internet Explorer with the enticing offer of free distribution. The message included a form letter sent to ISPs from Microsoft's Internet Business Development Group that read, in part: "I would like to have you distribute Internet Explorer for Win 95, Win 3.1 and Macintosh to your customers. We will license those products to you free of charge. I am also offering a copy of Internet Information Server which, I think, you as an ISP will find adds value to your service. The Internet Explorer offers you reduced browser costs, which should help you to differentiate your service, while allowing you to provide your customers with a great browser." (NSC 005804-005805)

146. AT&T WorldNet was a major ISP and one that Microsoft targeted heavily for an Internet Explorer exclusionary deal. In May 1996, Netscape's Fred Giordano sent an internal email about AT&T WorldNet: "The AT&T WorldNet agreement term has approximately 4 years remaining. We are competing against MS 'free,' as MS is offering the usual terms one would expect them to offer WorldNet (free Internet Explorer, free upgrades, presence on Win '95, free advertising space on MS home site, etc.)." (NSC 020298)

147. Even some distributors of Internet software felt that Microsoft's marketing tactics were unfair, despite the short-term advantages they gained. A September 1996 internal Netscape email shows that Gianni Comoglio of Olivetti's Telemedia Group "said that Netscape should take Microsoft to court ... as he felt Microsoft was being unfair in Microsoft's proposal to have Telemedia's ISP service to distribute Microsoft's Internet Explorer for free. He said the agreement ... allows Olivetti to get money in the form of a 'referral fee' each time Explorer is put on a CD that Olivetti distributes. ... Mr. Comoglio's pro-Netscape argument to his marketing management were initially rebutted because of the more attractive financial aspects of Microsoft's proposal." (NSC 019247-019248)

148. Microsoft's practices with regard to ISPs had a direct impact on Netscape. On June 7, 1996, a Netscape account manager sent an email to Netscape's Netsales Regional Sales Manager about ISP accounts he had lost to Microsoft. Inland Valley Internet Services and Source Internet Services were both described as start-up ISPs that chose Internet Explorer over Netscape's Navigator because it was free, even though they would prefer to distribute Netscape. (NSC 001968; NSMS 56733) In addition, at Burlington Air Express, "top management dismissed Netscape because IE is free." Id.

149. In June 1996 Netscape lost a distribution contract with an ISP called Global Telecom. The President of Global Telecom wrote that "Microsoft gave me a

deal I couldn't refuse. Free dialer, browser, developer kit, freely distributable, etc. . . . I know Netscape is better, but $0 vs $18K is impossible to beat." (NSC 002417)

150. On August 14, 1996, Netscape learned from Earthlink, a major ISP, that Earthlink was going with Microsoft because of Microsoft's control over the desktop. Earthlink described Microsoft's pressures and tactics as "medieval." Earthlink felt tremendous pressure to reach a deal with Microsoft to distribute Internet Explorer — and to give it preferential treatment — despite the fact that it feared Microsoft and the power it might exert over the Internet industry if it defeated Netscape. (NSMS 57009-57011)

151. In February 1997, Netscape learned that Microsoft had offered a New York ISP, Lightning Internet, free software, free hardware, and free advertising. Microsoft also offered to pay it commissions on sales of future Microsoft NT products. They "were panicked because customers wanted Netscape, but MS was pressuring with freebies, etc. He was pleading for our product free, logo free, and advertising free." Boston Consulting Group, Ultranet, Utilicorp, Eatel, and Clarity Communications are other companies that chose Microsoft because it offered free software. (NSC 015141-015145)

152. Mercury Internet Services wrote to Netscape on September 6, 1997: "We no longer give the Netscape Navigator Software away nor do we sell it. We have not been pleased that we can give away Microsoft's Internet Explorer free

and we have to pay for Netscape." (NSMS 025058-025060)

153. Bliss Advertising and Design advised Netscape it had stopped distributing Navigator on March 12, 1997. "We have stopped the use, support and distribution of Netscape to our customers," they wrote. "This was only to keep competitive. We still believe in your product but your direct competitor left us no choice. . . . I sincerely apologize if this is a trend." (NSMS 005801-005804)

154. Web Services Group, a small ISP, wrote Netscape in May, 1997 to acknowledge they had stopped distributing Netscape Navigator. Jim Gile of Web Services Group wrote that "for a smaller service provider like ourselves, it has become difficult to justify the cost of Netscape ($20 per copy) as compared to Internet Explorer at $0.00 a copy. . . . At this point we will no longer distribute any Netscape Navigator software. Thank you for help up to this point. And again, we regret that we have to make this decision and will continue to root for Netscape as it competes with Bill Gates crew." (NSMS 042728-042731)

155. On September 18, 1997, Doug McClure, Technical Project Leader of Scescape, Inc., an ISP in South Carolina, informed Netscape it had ceased distribution of Navigator. McClure wrote that "your product *is* excellent but totally lacking in marketing support and we could never justify the $20 setup cost when Microsoft will fly a blimp with our name on it for free. I sincerely wish

Netscape could compete with this but we are getting slammed by these costs, and this is the very thing that will kill your browser, which I incidentally prefer. We held out as long as we could but can no longer bear this tariff." (NSMS 034507-034511)

156. Mid Ohio Net informed Netscape in early March, 1997, that they were no longer distributing Navigator. Justin Cheen of Netscape called Mid Ohio Net to ask "if they wanted to distribute anymore and they said no way; not when the Internet Explorer is free." (NSMS 026727-026732)

157. Microsoft's practices have continued into 1998. In April of 1998, a complaint about Microsoft was posted to a Netscape newsgroup. The author forwarded an email sent to the webmaster of the ISP where he worked. He wrote: "Basically, Microsoft will give you two copies of NT and other software if you force over 500 of your users to use Internet Explorer. Frightening. Is this legal?" Even though Internet Explorer already was free, the e-mail from ecmail1@microsoft.com offered free copies of: Windows NT Server 4.0; Proxy Server 2.0; Windows NT Option Pack for each 500 users of Internet Explorer 4.0. (NSMS 63266-63267).

158. The impact of Microsoft's ISP licensing practices on consumers has been dramatic. Earlier this year, the consumer group NetAction published a report on "Consumer Choice in Web Browsers." Based on a June 1998 survey of top ISPs that provide service to consumers, the report stated that "The

disturbing reality is that the four largest retail Internet Service Providers, with a combined subscriber base of over 20 million customers, distribute only Internet Explorer to their customers." The report makes three additional points relevant to Microsoft's practices with the ISPs. First, although Microsoft, under pressure from the European Union and the Senate Judiciary Committee in February and March 1998, stated that it would not continue to enforce certain of the exclusionary provisions in its ISP contracts, "the damage had largely been done" by that time. Second, the report finds that with the incorporation of Internet Explorer into Windows 98, there will be increasing disincentive for ISPs to distribute a Netscape browser. And third, the report concludes that downloading browsers from the Internet is not as effective a method of distribution to ISP customers, especially computer novices, as is bundling by the ISP: "While Microsoft defenders note that consumers can download alternative browsers off the Internet, this is mostly a theoretical choice for computer novices, who tend to stick with the software provided by their ISP."

159. ***OEM Foreclosure*** – Netscape experienced early successes in getting OEMs to distribute the browser with computers. Some computer manufacturers installed Navigator on new machines; others provided Navigator on a CD-ROM included in the box with new machines.

160. OEMs were anxious to enter into agreements with Netscape because it

allowed them to differentiate their machines from those of other manufacturers and to add value for consumers. The OEMs that Netscape dealt with did not express concerns or have any difficulty installing the Netscape products on top of Windows.

161. Starting in 1994, Netscape entered into contracts to distribute Navigator with some of the world's largest OEMs. Netscape's first browser-distribution contract with an OEM was in November 1994 with Digital Equipment Corporation. Then, in 1995, Netscape entered into such contracts with a large number of OEMs, including Acer, Apple, AST, Compaq, Fujitsu, Hewlett-Packard, IBM, NEC, Siemens and Zenith. In 1996, we were able to sign two additional browser-distribution contracts, with Hitachi and Sony, but it was becoming increasingly difficult for us to get effective distribution through the OEMs due to the pressure being brought on them by Microsoft.

162. It was at that time that we began to get widespread reports to the effect that (1) OEMs were required to keep the Internet Explorer icon on the desktop (or lose their Windows license), (2) various financial incentives were offered to OEMs to get them to "prefer" Internet Explorer over Netscape Navigator, including discounts on the operating system and on other software, and (3) subtle and not-so-subtle verbal pressure was put on the OEMs not to have anything to do with us. A couple of OEMs even told us they could not put a "Netscape Now" button on their own home page due to restrictions in their

Microsoft contracts.

163. Further, I was told that senior executives of Microsoft, including Bill Gates, called the CEOs of certain OEMs to warn them that there would be negative consequences resulting from their doing business with Netscape.

164. One such incident occurred after Netscape and Hewlett-Packard announced a joint product marketing arrangement at a press event. We learned from Rick Belluzzo, then of Hewlett-Packard, that both Bill Gates and Steve Ballmer had called Hewlett-Packard after the event and had expressed displeasure over the announcement. I heard similar reports directly from CEOs of other types of businesses, such as Dave Dorman, who received a call from Mr. Ballmer after PacBell Internet Service signed a contract with Netscape. In that call, Mr. Ballmer told Mr. Dorman he had become "an enemy" of Microsoft by doing business with Netscape. This call was subsequently reported in The Wall Street Journal. (10/27/97, "For Microsoft, the Phone is a Potent Weapon," p. B1.)

165. Our salespeople also told me that the OEMs were offered a discount on Microsoft products, including Windows, if they would make Internet Explorer their "preferred" browser, and that certain OEMs that tried to put Netscape Navigator on their machines alongside Internet Explorer learned that they would lose valuable marketing dollars provided by Microsoft if they did so. My salespeoples' reports were consistent with press reports that the PC

makers were being pressured by Microsoft. In "PC Makers: Microsoft used Pressure Tactics," reported in PC Week, August 26, 1996, seven different OEMs said Microsoft "used various pressure tactics to emphasize Internet Explorer over Netscape Navigator," including threatening to re-evaluate Windows 95 licensing fees if Netscape Navigator were bundled on their computers, withholding participation in marketing programs if vendors bundled both Netscape Navigator and Internet Explorer, and threatening to raise the Windows 95 licensing fee if Internet Explorer 3.0 were removed from the operating system. Once this Microsoft pressure on the OEMs started, it became much more difficult for us to close any business deals, and particularly business involving our browsers, with the OEMs.

166. The OEM incident that most unsettled me involved Compaq. We had had a very good working relationship with Compaq. In fact, one of Compaq's Vice Presidents, Ronnie Ward, spoke in very complimentary terms about Netscape, the Internet, and Java at one of our developers' conferences. (Interestingly, Mr. Ward later told one of our salespeople that because he had referred to Java during his presentation as "letting the world out of jail," Microsoft had questioned his and Compaq's loyalty to Microsoft and this had upset certain senior managers at Compaq.) In addition, Compaq had agreed to distribute the Netscape Navigator on its popular Presario line, and Compaq personnel were enthusiastic about putting an icon for the Netscape

Navigator on the Presario desktop. At one meeting, a group from Compaq showed some of our employees a preliminary build of the Presario product, happily pointing out that the icon for the Netscape Navigator was on the desktop. However, when the final build of the Presario product shipped in 1995, we found to our amazement and dismay that the icon for the Netscape Navigator was not on the desktop. We learned from a Compaq product manager that Microsoft had not wanted Compaq to put the Navigator icon on the desktop, even alongside the Internet Explorer icon. We also learned that Microsoft had threatened to terminate Compaq's Windows license. This would have put Compaq -- the largest PC OEM in the world -- out of business. This demonstrates Microsoft's unprecedented power. The effect of this pressure from Microsoft was to destroy the value of our contract with Compaq.

167. In 1997 our salespeople tried again to get Compaq to ship Navigator on their Presario line, but they were told by the Presario personnel that they could not work on a new contract with us until over a year later, after they had concluded the renegotiation of their Windows license with Microsoft. They indicated they were sensitive about working with Netscape because doing so in the past had caused friction in their relations with Microsoft. This was consistent with what we had understood from various Compaq personnel, including Compaq's CEO, Eckhard Pfeiffer with whom I met personally and

discussed this during 1996 and 1997.

168. NCR provides an example of Microsoft offering cash discounts on Windows in exchange for adopting Internet Explorer. I understand that Microsoft provided NCR with a "market development agreement" that ties royalty reductions to NCR's putting the Microsoft logo on NCR's homepage, using Internet Explorer, and hotlinking to the Microsoft homepage. I understand that under the agreement NCR is not allowed to modify Windows screens in any way, including deletion of the Internet Explorer logo, or to change the "boot-up" process (to permit it to load Netscape Navigator). We were told that NCR put the Internet Explorer logo on its homepage and, to be fair, put the Netscape logo on as well. We were told that Microsoft then called and said that Microsoft management looks very negatively at NCR putting the Netscape logo there and if NCR wants to partner with Microsoft, NCR should not do that. In addition, after the NCR/Netscape press release in the first week of August of 1996, I understand that Microsoft told NCR that Netscape was Microsoft's number one competitor and that Microsoft and NCR's licensing relationship was going to get a lot harder. In addition, we were told that a Microsoft sales person said that Microsoft has a "revenue maximize" list that includes companies that are less than fully cooperative, and that justifies price differences to these companies because, he said, Robinson-Patman price discrimination restrictions don't apply to software. (NSMS

56979-56980)

169. In addition to the pressure being exerted by Microsoft on OEMs, we learned of other Microsoft practices to restrict our access to the OEM channel. On September 5, 1996, IBM informed Netscape that Microsoft created "new restrictions in the Windows 95 license agreement which prevent any OEM from modifying the default desktop or 'shell.'" This would lock OEMs into Nashville (the Code name for Windows 98) and shut out OEM-specific shells such as the Packard Bell interface, and the IBM Aptiva interface. (NSC 070784-70788)

170. Microsoft threatened PC manufacturers in other ways. Gil Amelio informed Netscape that Apple had to agree to bundle Internet Explorer along with Netscape, because Bill Gates would only develop Office 97 for the Mac OS/Next OS platform if Apple bundled Internet Explorer. (NSC 002202)

171. AST reported that it was very concerned about choosing Netscape Navigator as its browser, because it believed that Microsoft could easily raise the price of the other software programs that AST buys from Microsoft. (NSC 002305)

172. Several OEMs in Japan complained to Netscape that Microsoft threatened that if the OEMs use Navigator, Microsoft would increase the royalty license fee for Windows. (NSC 000150)

173. Today, Netscape has limited distribution agreements with some OEMs. None of these agreements provide effective mass distribution outlets, as all of our

agreements are engineered around Microsoft's restrictions. For example, our contracts are restricted as follows:

- -- IBM: offers Netscape browser on the Aptiva and ThinkPad lines, but without a desktop icon. As in most cases, Internet Explorer has a desktop icon on those lines;
- -- Gateway: provides Netscape browser through a separate compact disk;
- -- Sony: offers Netscape on some limited lines, but without a desktop icon;
- -- Apple: offers Navigator on the iMac, PowerMacs, and PowerBooks, but without a desktop icon;
- -- NEC: offers Netscape browser on a CD on one notebook computer;
- -- Fujitsu: offers Netscape browser with LifeBook notebook;
- -- Hewlett Packard: offers Netscape browser with Kayak PC workstations (one of its smaller lines);
- -- The Netscape browser is effectively not distributed at all through the largest OEMs (Dell, Compaq), or on Packard Bell, Acer, Toshiba, or Micron.

174. ***ISV Foreclosure*** – Independent software vendors have also been an important distribution channel for Netscape software. Specifically, ISVs, who had their own established distribution channels, would agree to distribute our software along with their software. Microsoft has tried to eliminate the ISVs as a meaningful distribution channel for Netscape.

175. In particular, I have experienced Microsoft's ability to use its monopoly power to foreclose our opportunities with an ISV as we tried to negotiate a deal with

Intuit. We expended enormous amounts of time and energy trying to work with Intuit. Intuit needed an embeddable browser for its Quicken product. It had very specific requirements. Intuit needed the ability to display web pages without any of the surrounding user interface elements of the browser. We worked with Intuit for months to determine if our stand-alone browser could provide the user interface it needed. My understanding is that we had offered Intuit several technical options that it agreed would meet its needs. However, despite the progress we were making, I began to suspect that Microsoft was exerting extreme pressure on Intuit. In 1997, Intuit informed us that it felt that it had no choice but to do an exclusive deal with Microsoft.

176. Obviously, we felt that we had come so close to getting the Intuit deal, we were all quite disappointed to not get it. In fact, I instructed Danny Shader, Netscape's Vice President of Development Relations, to prepare an analysis, at the time, to help us think about what we could have done better to get the Intuit deal. As I do at many important junctures in our business, I asked my staff to discuss with me what we did right and what we did wrong regarding Intuit.

177. At the time, some on my team believed that the reason that we didn't get the Quicken deal was because Intuit found Microsoft's engineering solution preferable to ours. Although they were issues, I have never believed that our product or engineering design were the primary issues in the Intuit deal.

178. My understanding is that Microsoft coerced Intuit into adopting its technology. Intuit later informed us that Microsoft was offering the inclusion of Quicken code into Windows and the display of Quicken.Com on the desktop. I believe Microsoft's unique ability to place Quicken on the Windows desktop and the vast opportunity that access to the monopoly desktop would give Intuit was the reason Intuit went with Microsoft.

179. My conclusions with regard to Intuit are not surprising given the other stories I was hearing at the time. I learned that Microsoft threatened Attachmate in 1996, after Microsoft learned Attachmate was planning to release a "TCP/IP gateway product that was directly competitive with a Microsoft product. They also learned that Attachmate was bundling the Netscape Navigator with their various products. ... Microsoft therefore contacted Attachmate and told them that Microsoft would start bundling 3720 emulation software (directly competitive with Attachmate's emulation software) into the operating system unless Attachmate took the following actions: (1) cease working on the TCP/IP gateway, and (2) stop distributing NN. ... As a result of these threats, Attachmate has stopped all work on the Gateway project. ... In addition, Attachmate will no longer distribute NN." (NSMS 57057)

180. Quarterdeck was an ISV that considered Navigator technically equal, if not superior, to Internet Explorer, but was dissuaded by the price difference. A

Quarterdeck VP wrote to Ram Shriram: "We are considering Microsoft Internet Explorer and Netscape Navigator. There is no question that Navigator is at no disadvantage on the features checklist. However, we do need for the economics to make sense as well given the competitive nature of the Internet space." (NSC 019014-019015)

181. ***ICP Foreclosure*** – Internet Content Providers also provide a meaningful method of distribution for Netscape. Netscape started its "Netscape Now" button campaign in 1995. The "Netscape Now" button is what content providers put on their web pages to facilitate download of Netscape Navigator or Communicator. While this means of distribution is nowhere near as beneficial as the OEM and ISP channels because of the limitations on downloading discussed below, it is still an important means of distribution. In this channel, Microsoft also offered ICPs "better than free" terms to enter into exclusionary deals with Microsoft. Even more importantly, Microsoft again offered desktop placement in exchange for exclusionary deals. Specifically, Microsoft targeted some of the nation's most popular sites with desktop placement through its "channel bar" in exchange for its exclusionary deals.

182. One significant example comes to mind: Disney. Disney.com is one of the most popular sites on the Web. In exchange for placement on the Windows 95 channel bar, Microsoft was able to extract an exclusionary deal with

Disney. Netscape had been in negotiations with Disney to place Disney.com on our "Netcaster" channel bar that existed at that time. Disney had expressed, quite naturally, interest in the broadest possible placement of Disney.com; it would obviously be in Disney's interest normally to be placed on more than one company's channel bar. However, as we were concluding contract negotiations with Disney, it became clear to my team that Disney was likely to sign an exclusionary deal with Microsoft. Disney told us they would have liked to do a deal with Netscape, but as a condition of their Microsoft contract for placement on the Windows desktop, Disney was prohibited from offering Netscape compensation of any kind! Disney would also have been prohibited from promoting, even informing customers, or even letting us promote, the Disney.com placement on Netscape's products.

183. Microsoft was able to extract other exclusionary deals. In August 1996 the popular web site ESPNet Sportszone refused to display the "Netscape Now" button on its site. According to an e-mail by Barbara Gore of Netscape, "that refusal was because of the contract they have with Microsoft. Brian will email us on the exact wording they are using, something like 'recognized revenue' they are providing to ESPN for their deal. (They are BUYING content providers!, to be exclusive with them.") (NSC 070693-070694)

184. CNet started a web site in 1996 called "download.com," for which it was selling advertising during that year. Bill McGee of Netscape's advertising

agency reported in September: "When I asked about the availability of the button for Netscape, I was told that Microsoft had made a substantial commitment to download.com, in particular, and CNet, in general, which included 'browser exclusivity' on these download buttons - other companies such as RealAudio and Macromedia would be able to purchase buttons, but no one offering a browser." (NSC 012079)

185. An internal Netscape email from January 1997 relayed a conversation with Allen Loren of American Express. Loren told Kristofer Younger of Netscape: "We went with Microsoft not because of their technology, because yours is better, but because they could be a better distribution channel for me. I can put my stuff on every copy of Windows 95 or 97 or whatever." (NSC 015042)

186. Microsoft also provided compensation to content providers to promote and distribute its free product. In July 1996 Netscape employees received a report that Microsoft was "approaching large web sites that charge for portions of their content ... offering to subsidize the cost of paid-for content, if end-users are using Internet Explorer to access that content." (NSC 002048)

187. A January 1997 internal Netscape email discussed Microsoft's marketing tactics with Intelligent Electronics, a Colorado distributor that allows resellers to order products directly from the Internet. Intelligent Electronics told Netscape that "Microsoft offered ... free product and $100,000 to develop the system with Microsoft BackOffice. In exchange he would have had to

agree to run the system exclusively using MS BackOffice and Internet Explorer, and he would have to advertise on his website that the site was powered with MS BackOffice." (NSC 002345)

188. An August 15, 1996 email revealed a case in which Microsoft offered cash to a company that planned to customize its web site toward Microsoft technology on an exclusive basis. Jonathan Shapiro of United Media, the distributor of the Dilbert cartoon strip, "said that Microsoft offered them money and promotion in exchange for customizing to Microsoft's technology on an exclusive basis." (NSC 002162)

189. A June 1996 internal Netscape email about Toys R Us reveals that the toy company at that time was planning a major overhaul of its web site, and Microsoft was very aggressive in trying to get adoption of Internet Explorer technology. Microsoft offered Toys R Us several hundred thousand dollars worth of free consulting in exchange for the company using Internet Explorer technology. (NSC 001835)

190. Microsoft was pushing the display of the Internet Explorer logo very strongly to web sites in Europe. A form email from Microsoft made the following offer: "In return for your displaying the Internet Explorer Logo on your site, Microsoft UK will send you a *free* copy of the 'Mastering Internet Development with ActiveX Technologies' CD worth 79 pounds. What's more, your site will be listed on the Microsoft UK web site." (NSC 005845-005847)

191. ***Corporate Account Foreclosure*** – Corporate customers are very important to Netscape. Direct sales to such customers resulted in a substantial portion of our revenue. Microsoft interfered with Netscape's direct sales efforts to Corporate Accounts through direct pressure, leveraging the power of its operating system monopoly, and again, free and better than free offers.

192. Netscape was trying to enter the corporate Intranet market in 1996. Corporations use intranets for internal communications, and the browser is an essential component to these systems. According to Mark Tyler of Netscape, Microsoft was doing everything it could to keep Netscape out of the market. "Acer Computer in Taiwan is our first real Intranet deal ... or at least it would be if Microsoft weren't trying to keep us out at any cost. They have given Acer a killer price on an upgrade to Win95 from Win 3.1 if they will use Internet Explorer exclusively and not Netscape Nav. ... A win is doubtful. How low can we go in price to counteract a free browser, and an upgraded operating system at a dirt low price?" (NSMS 56766)

193. In the fall of 1996, KPMG Peat Marwick ("KPMG") tested the intranet products offered by both Netscape and Microsoft. After KPMG completed this evaluation, I was informed that Netscape won the technical comparison and that KPMG had selected Netscape to develop its intranet for its U.S. offices. KPMG also agreed to help many of its large corporate clients install Netscape intranets, which could have helped to increase browser distribution.

Netscape was paid in full upfront and the deal was announced on January 24, 1997.

194. In response to that announcement, I understand that Jeff Raikes, the head of sales at Microsoft, immediately contacted KPMG vice chair Roger Siboni. After a February 1997 breakfast meeting between the two of them, Mr. Siboni contacted me to inform me that KPMG was reevaluating our systems. Mr. Siboni told me that in March Microsoft invited Mr. Siboni and his information technology group to Microsoft's executive briefing center in Redmond, Washington where they had a forty-five minute meeting with Bill Gates. I understand that while Mr. Siboni was in Redmond, Microsoft made a proposal to partner with KPMG in electronic commerce and the automation of sales force procedures so that both companies could better compete with IBM and Oracle.

195. I understand that KPMG and Microsoft still had problems reaching an agreement, because KPMG operated a mix of Windows 95, Windows 3.1, and Macintosh systems, much of which would be incompatible with the Microsoft intranet services. Implementing Microsoft's products would require a full software and hardware upgrade. Netscape, on the other hand, offered a cross-platform solution at a lower total price. In addition, I understand that there was skepticism within KPMG on whether Microsoft would be able to meet KPMG's deadline. Thus, on June 2, 1997, Mr. Siboni called me to say

that it appeared that Netscape would again win the contract, but he asked me to remain quiet so that he could explain the decision to KPMG's foreign partners and could inform Microsoft.

196. In response to KPMG's rumored decision to use Netscape software, I understand that Microsoft agreed to include KPMG in a "rapid deployment" program that would give it early access to Microsoft's software and promised to speed up work on Macintosh compatible versions of its software. Mr. Raikes also offered further discounts if KPMG implemented Microsoft's system globally. Microsoft then offered to buy a 10% stake in Enterprise Integration Systems, a KPMG group that resells networking technology. Microsoft offered $10 million dollars to cover most of the start-up costs of a new KPMG unit that would sell services implementing Windows NT. Some of this investment would be repaid from future revenues of the Windows NT unit, while the remainder (for promotional and marketing expenses) would not have to be repaid. Finally, Microsoft agreed that if it missed its implementation deadline, it would forgive a greater part of the investment in the Windows NT unit.

197. KPMG accepted this deal with Microsoft. On July 15, 1997, Mr. Siboni called to inform me that the agreement with Netscape would be rescinded. This was shocking to me, given the investment KPMG made in Netscape products and the commitment I thought we had with them.

198. Other Netscape documents provide further examples of Microsoft interference with Netscape browser distribution to Corporate Accounts. Cate Townsend, an information services officer at a company that licensed Internet Explorer, wrote to Microsoft in late January, 1996, to determine whether the company's Microsoft license agreement restricted its right to distribute another browser. Jeff Tran of Microsoft's Internet Explorer Team responded that "you must distribute Microsoft Internet Explorer V. 2.0 as the only browser for Win95 users. If you plan on distribution to Win3.1 or Macintosh users another browser may be distributed, however the beta version of MSInternet Explorer [is] available for Win 3.1 and Mac users to download off our website." Townsend later forwarded these two e-mails, along with the relevant language from the company's Internet Explorer license agreement, to Netscape. (NSC 002124-002125)

199. A different approach by Microsoft was seen in New Zealand, where Microsoft offered to upgrade Telecom New Zealand's 9000+ Win 3.1 terminals to Windows 95 for free if Telecom would use Internet Explorer as its internal browser. (NSC 001948)

200. An email to Netscape from a small microbrewery in June, 1996 prompted the concern of Netscape's Judy Logan. Here was a "relatively small site" being given "free exposure in print advertising" by Microsoft; in addition, "Microsoft has offered $1000 of free software, Microsoft has guaranteed co-marketing

activities for the next year," and "an explicit term of the agreement is to remove any reference to Netscape from their site." (NSMS 56772)

201. Netscape saw much growth potential in international corporate markets by 1996. After visits to Netscape's major accounts in Brazil, Netscape learned that Microsoft was visiting all the same companies and offering the following: "pay $1.00 to take each navigator out of the account"; "support and provide all of their products and give mktg dollars to support vendors in trade shows, conferences etc"; "give MS Explorer for free for 2 years"; "work with the key accounts to do whatever they can to promote MS's products (i.e. mktg dollars, MS resources at shows etc)"; "give free servers and Explorer to banks." (NSC 019334)

202. In July 1996 representatives from Microsoft met with International Paper, hoping to license its Internet/Intranet software. In the aftermath, John Pullen of International Paper wrote to Netscape: "Unfortunately, the fact that they are offering us all of their Internet/Intranet software (with the exception of say an Exchange server and some tools) for free is a big obstacle for Netscape. That 'free' word happens to pull a lot of weight around here. We need to get you guys to come up with something pretty soon so that we don't end up getting sucked into MS's web." (NSC 002015)

203. A July 31, 1996 internal Netscape email reported a comment from an employee of QVC, the substance of which was that QVC was "using

Microsoft's IIS and Explorer because MS paid them 'a whole lot of money' in a big deal they did together." (NSC 002017)

204. An August 8, 1996 internal Netscape email states that Microsoft, in response to a marketing package whereby BTG was including the Navigator browser on 32-bit Windows systems shipped to federal agencies, informed BTG that "they would drop the price for Win 95 and/or NT if MSInternet explorer were configured instead of Netscape Navigator." (NSMS 56981)

205. **Other Microsoft Conduct Aimed at Eliminating Netscape as a Competitor** – Other conduct by Microsoft has substantially impaired Netscape's ability to compete. Most notably, Microsoft has delayed entering into licenses of essential Microsoft code necessary for Netscape to innovate or develop products to work with Windows. Moreover, elements of Microsoft code have created unnecessary technical problems or conflicts in several instances for our rival browser.

206. Microsoft has delayed providing technical information to Netscape or entering into licenses of essential Microsoft code, in some cases with the effect of delaying product development or release or foreclosing us from doing business with certain ISPs.

207. For example, in 1996, we began trying to license a scripting tool for Windows 95 dial-up networking, which we hoped to include in new versions of Personal Edition and Dial-Up Kit. This tool was especially important to us because

some ISPs, but not all, required scripting. At that time, accessing the Internet was not as easy as it is today. Our goal was to make Internet access as easy as possible for persons using our browser. If we did not have the scripting tool, it was very difficult for computer users with our browser to access the Internet through some ISPs.

208. Despite our repeated requests over the next few weeks, Microsoft took no action on the matter. We believed that the scripting engine was readily available. John Freeborg, a Netscape employee, confirmed that fact by making up the name of an ISP and getting on Microsoft's ISP mailing list, using his home address. On June 28, 1996, Freeborg received a packet from Microsoft explaining that the scripting engine we were requesting was available to ISPs for redistribution on a royalty-free basis if the ISP signed a Microsoft license that, among other things, required the ISP to use Internet Explorer as the "preferred web browser," issue a press release announcing the licensing, and use the Internet Explorer logo. (NSC 005813)

209. By mid-July, both Netscape's legal department and Microsoft's legal department had approved the licensing agreement under which we sought the scripting tool. Rick Schell signed the agreement on Netscape's behalf on July 18, 1996. The agreement was forwarded to Microsoft for signature.

210. Microsoft had not signed the agreement by July 25, 1996. On that day, Freeborg again spoke to Ed Mitchell of Microsoft, conveying our great

frustration about Microsoft's delay in signing the license agreement and in failing to provide us with a scripting tool that Microsoft was already freely distributing to ISPs. Freeborg asked Mitchell for a commitment that Microsoft would sign the license agreement that week. Mitchell refused. (NSC 000176) Meanwhile, Netscape got numerous complaints that we were not distributing ~~this~~ tool that was already widely available. (NSC 002007)

211. Mitchell subsequently informed Freeborg that Brad Silverberg, Microsoft's Senior Vice President Personal Systems Division, had some concerns over Netscape's licensing of the scripting tool. Freeborg and Julie Herendeen, another Netscape employee, attempted to contact Silverberg but were unsuccessful. By e-mail to Silverberg, Freeborg again expressed Netscape's desire to speed up the licensing process and asked if there were any specific issues Netscape could address in order to expedite Microsoft's execution of the license. (NSC 000177)

212. On August 14, 1996, Freeborg and Herendeen spoke to Will Poole of Microsoft. Poole advised them that Microsoft's Paul Maritz had written a letter to Rick Schell listing a number of open issues between Microsoft and Netscape (one of which was the scripting license) on which Microsoft felt both parties could be more cooperative. Poole said that Microsoft was unwilling to discuss the scripting license as a separate issue. (NSC 000181)

213. Because Microsoft refused to address the issue separately -- without Netscape

being more "cooperative" on other issues -- we were never able to license the scripting tool. Although Netscape and ISPs were eventually able to work around this problem, Microsoft's refusal to license the scripting tool to us -- a tool that was freely available to others for redistribution on a royalty-free basis -- effectively foreclosed Netscape for a period of time from doing business with those ISPs, such as Sprynet, that required scripting. In that interval, Microsoft signed a number of deals with those same ISPs making Internet Explorer the "preferred" browser.

214. In addition, Netscape has discovered and been informed of numerous technical incompatabilities that appear to have been designed to prohibit access to certain information by Netscape users. On June 10, 1996, I was informed that Microsoft Developers Network (which provides information to software developers about Windows so that developers can ensure that their applications are compatible with Windows) required the presence of Microsoft Internet Explorer to be fully functional. It would not function with the computer user's preferred browser. (NSC 001967)

215. On August 13 1996, Netscape discovered that users attempting to visit the site at the URL http://home.microsoft.com with a Netscape Navigator were denied access. To obtain access, the user needed Internet Explorer. (NSC 0002092-002093). Microsoft later corrected this in response to press accounts.

216. We also learned of other technical problems and conflicts from persons outside the company, most notably Netscape customers who were having difficulties using our product because of conflicts created by Internet Explorer or other Microsoft products. For example, in November 1996, Netscape was informed by a customer who had upgraded to NT 4.0 Server, and installed the accompanying IIS 2.0 Microsoft server (replacing Netscape's IIS 1.0 server), that the immediate result was that any user surfing to the customer's web site with a Netscape browser was challenged to enter a user name and password, and then was given an "access denied" message. That user was denied access even if he or she had a valid name and password with full administration privileges. The customer then searched the Microsoft web site looking for some kind of help. He found a document that mentioned this problem and improperly attributed it to the inability of "Netscape browsers [to] properly handle an NT challenge/response." (NSC 001665)

217. In December 1996, Michael Hawkins, a Netscape OEM & Strategic Technical Support Engineer, was informed by an ISP that had just installed a Microsoft NT server running Microsoft IIS about a problem using Netscape Navigator. Apparently, all of the ISPs who used Internet Explorer could use the server product, but Netscape Navigator users could not successfully log in at all. Hawkins called the customer and discovered that by specifying "basic text" on the server's access control setting, rather than following Microsoft's

recommendation, all users could access the IIS server regardless of the browser used. (NSC 002204-002208)

EFFECTS OF MICROSOFT CONDUCT

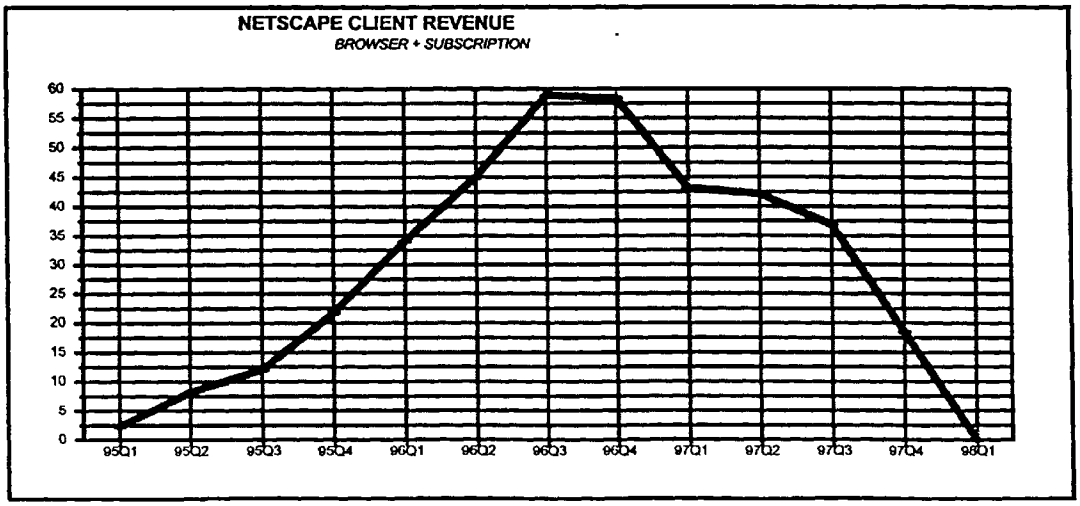
218. I have reviewed above numerous examples of Microsoft's anti-competitive conduct, including specific instances in which Netscape lost business because of Microsoft's exclusionary and predatory practices, pressure, and "better than free" offers. This conduct has had a serious detrimental effect on the ability of Netscape, or any other browser company, to compete, and it has limited consumer choice. The two most objective ways in which to measure the cumulative effect of Microsoft's conduct are through tracking revenue over time and tracking market share over time. The detailed discussion of each of these issues below clearly demonstrates that Microsoft's plan to "crush" Netscape in the browser space unfortunately is becoming increasingly effective.

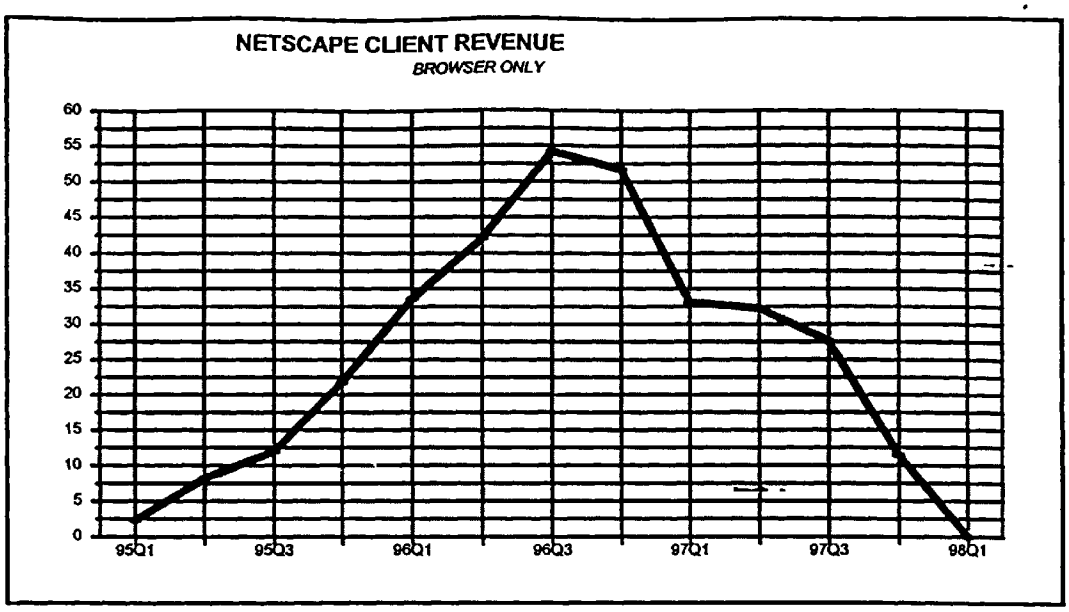
219. **Revenue** – During 1995 and much of 1996, Netscape's primary revenues came from licenses of our browser. Those license fees escalated significantly, from $2.3 million in the first quarter of 1995 to $58.5 million for the fourth quarter of 1996, and were projected to continue trending upward. However, by 1997, Microsoft's constriction of Netscape's distribution channels had begun to reduce significantly our ability to receive revenues from new licenses of the browser. The following chart demonstrates the growth,

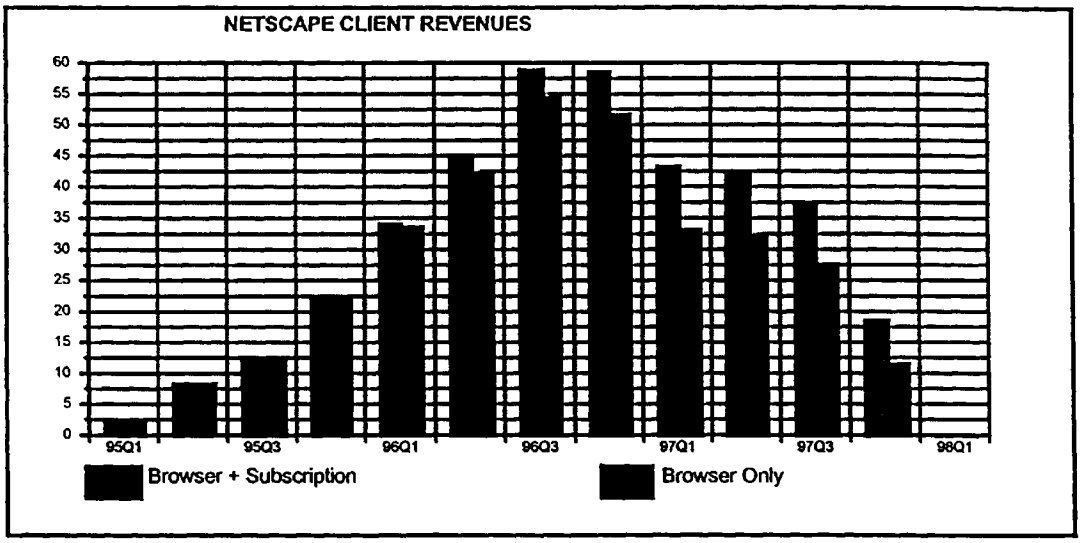
flattening, and decline of revenues from Netscape's browser through the first quarter of 1998:

1995	Q1	Q2	Q3	Q4
Browser + Subscription	$2,326	$8,245	$12,010	$21,779
Browser Only	$2,326	$8,245	$12,010	$21,779
1996	Q1	Q2	Q3	Q4
Browser + Subscription	$34,072	$45,052	$58,867	$58,466
Browser Only	$33,557	$42,130	$54,248	$51,710
1997	Q1	Q2	Q3	Q4
Browser + Subscription	$43,145	$42,112	$36,869	$18,523
Browser Only	$33,119	$32,247	$27,635	$11,523
1998	Q1	Q2	Q3	Q3
Browser + Subscription	$0			
Browser Only	$0			

220. These figures include licenses from Netscape Navigator and, beginning in June of 1997, Netscape Communicator. The total for "Browser + Subscription" reflects all revenues from stand-alone licenses of the browser plus revenue recognized from subscription fees under licenses from prior periods. The total for "Browser Only" reflects just revenues from stand-alone licenses of the browser, reflecting the new revenue-generating licenses entered into in a given quarter. Thus, "Browser + Subscription" is a trailing indicator, including revenues derived from past licenses, know as subscription fees which are allocated over different quarters for the length of the subcription; "Browser Only" more accurately demonstrates the precipitous decline in revenues from new browser licenses in each period. Both Browser + Subcription Client Revenue and Browser Only Client Revenue are plotted separately below, followed by comparison showing the more precipitous drop in new user browser licensing revenues:







221. In January 1998, as a result of Microsoft's actions, Netscape announced that it was making its browser available for free, and thus ceased receiving any material revenues from browser licenses.

222. **Market Share** – Netscape's browser market share has been dropping rapidly as Microsoft's exclusionary contracts and other predatory practices

took effect. According to the best data available to Netscape, our browser market share has dropped from over 70% in the first quarter of 1996 to approximately 40%-50%, currently, based on various studies. Moreover, these numbers understate the true effects of Microsoft's conduct, because our large installed base slows the statistical drop in overall market share, even as Netscape's market share of new browser users plummets. In fact, Netscape's share of new users has dropped much more significantly while Microsoft's share increased dramatically during the same period. Absent new developments, those numbers likely will result in further erosion of Netscape's overall market share as the installed base effect disappears over time.

223. The end result of Microsoft's practices is not just a drop in Netscape's market share and revenue; the end result, if Microsoft completely succeeds, is to deprive consumers of valuable innovations in this rapidly growing area of technology. Given that Netscape already has been forced to reduce its licensing fee to zero, it is deriving no revenue from browser licensing. Thus, although Netscape still chooses to invest in browser development, borrowing funds from other areas of the business, clearly this path will be difficult to sustain if Microsoft continues on its current path and accomplishes its goal.

224. Marc Andreessen recently found on the Internet an old letter written by Bill Gates in which Gates himself best described the effects on future innovation

of making software free -- what Microsoft began to do 20 years later. Back in 1976, when he and Paul Allen were just starting Microsoft, Mr. Gates wrote an "Open Letter to Hobbyists" relating to some improved versions of BASIC that he and Mr. Allen had invested $40,000 in developing. Mr. Gates was apparently irritated that many software hobbyists were using his improved BASIC -- and liked it -- but were not paying the licensing fees. Mr. Gates wrote:

> One thing you don't do by stealing software is get back at MITS for some problem you may have had. . . .One thing you do do is prevent good software from being written. Who can afford to do professional work for nothing? What hobbyist can put 3-man years into programming, finding all the bugs, documenting his product and distributing it for free? ("An Open Letter to Hobbyist," William Gates, III, February 3, 1996 as reprinted in the New York Times, July 23, 1997).

225. **Causes of Reduced Revenue and Market Share** -- There is no doubt in my mind that these drastic effects on our revenues and market share are the result of Microsoft's conduct described above. On the revenue side, all our browser revenue disappeared because it became increasingly difficult to charge for a product that our principal competitor was offering for free or "better than free," and we had been effectively locked out of the OEM and ISP distribution channels.

226. No other distribution channel today can make up for the loss of the OEM and ISP channels. While Netscape achieved significant successes in distribution

channels other than the OEM and ISP channels in the early years of the Internet, each alternative distribution method now suffers from several flaws or limitations.

227. Downloading is not an effective mass distribution mechanism today, because it takes a substantial amount of time and users have to be fairly sophisticated actually to download and install a browser. In the early days, most Internet users were quite sophisticated technically, and downloading a browser was feasible for them. Today's new users are, by and large, much less technically proficient, and the download process is daunting. While Microsoft has argued that statistics show that a significant number of people continue to download Netscape's products, these numbers need to be carefully evaluated, since the recorded numbers represent download attempts (many of which fail for technical reasons) and do not reflect whether that attempt resulted in the successful installation of a browser. In today's maturing Internet market, the OEM and ISP channels -- which are by far the easiest way for beginning users to obtain a browser -- have become the most important sources of current distribution.

228. Similarly, "carpet bombing" -- or mass distribution of unsolicited product -- is not an effective means of distribution for a browser company. First, it is extremely expensive. The high costs of carpet bombing do not make sense in the context of a software company that only earns a one-time fee for its

product, as opposed to an ISP that receives a monthly fee. Moreover, the high costs of carpet bombing are compounded by the fact that carpet bombing traditionally results in only a 1-2% adoption rate. Most unsolicited CD-ROM's end up in the trash, or as coasters that serve no purpose other than keeping the recipients' coffee cups from staining their desk. AOL is often cited as an example of successful carpet bombing. I would agree that the AOL carpet bombing experience was a success. However, AOL had to send out something like a billion -- 1,000,000,000 -- CD-ROM's to get something like a million subscribers. Moreover, AOL also gets a monthly subscription fee for its service, and thus has the potential to recoup its initial costs over time. For these reasons, Netscape has never carpet bombed and has no plans to do so in the future.

229. Netscape also distributes its products to some extent through ISVs, peripherals manufacturers, Value Added Resellers, or VARs, systems integrators and possibly others. Attempts to distribute through these alternatives to the OEM and ISP channels have been somewhat successful. However, that success must be put in context. Even a successful distribution arrangement with a peripherals manufacturers -- say, for example, a printer manufacturer -- will result in a very limited number of new browser users and is not going to make up for being excluded from distributing our product through the world's largest OEMs and ISPs.

230. In January of 1998, after we decided to make our browser free, we launched an "Unlimited Distribution" campaign, devoting tremendous resources to utilizing all available channels of distribution to increase our browser market share. While we obtained many new users from that effort, our overall maket share has continued to drop. Unfortunately, this simply confirms my view that in today's market there is no substitute for the OEM and ISP channels of distribution, which Microsoft has largely blocked through the predatory conduct discussed above.

231. Microsoft has publicly alleged that Netscape's loss in revenue and market share is a result of our failure to innovate. Nothing could be further from the truth. Netscape has been and continues to be a market leader with regard to browser innovations. Indeed, the 1.0 release of Navigator delivered incomparably better performance than other browsers available at the time. Its innovative capabilities included continuous document streaming, enabling users to interact with documents while they were still being downloaded rather than waiting for the entire document to load; multiple network accesses, allowing several documents or images to be downloaded simultaneously; native support for the JPEG image format; and security features such as encryption and server authentication.

232. Of course, because Navigator was available seven or eight months before Internet Explorer and before, to my knowledge, Microsoft had even

formulated its Internet strategy, Microsoft had a target to shoot for with its first release. Microsoft did not hit that target. Microsoft's 1.0 release of Internet Explorer was substantially inferior to Navigator's 1.0 release.

233. At the same time Microsoft was releasing Internet Explorer, Netscape was well on its way to its 2.0 release of Navigator. Navigator 2.0 and Internet Explorer 1.0 overlapped in the market for some period of time until Microsoft released Internet Explorer 2.0 in December of 1995. Again, reviews consistently ranked Netscape Navigator 2.0 as superior to Microsoft's later Internet Explorer 2.0 release.

234. What is most significant about Navigator's superiority to Internet Explorer during this period is that, even though Navigator's superiority was unquestioned by independent analysts and the public, Microsoft was able to begin gaining substantial market share at this time through its forced bundling with Windows 95, its exclusive deals, and other predatory practices.

235. Microsoft did not reach parity with Navigator 3.0 even as of the release of Internet Explorer 3.0 in August of 1996. Netscape had the lead in numerous important areas. These included LDAP and e-mail features, HTML composition, calendaring, cross platform support, open standards support, content security, HTML and VRML rendering performance, web site integration, memory utilization, stability, compatibility with other Windows applications, plug-in support, and download size.

236. The 4.0 release of Internet Explorer in September of 1997, released after Netscape's Navigator 4.0, was the first time that Microsoft reached anything resembling a level of parity with the then-current release of Navigator. The features and functionality of Navigator 4.0 and Internet Explorer 4.0 are similar, and the two products have both received positive reviews. While we believe our product is better, new users are unlikely to undertake a meaningful comparison if the only browser they receive, by virtue of bundling or exclusive arrangements with OEMs and ISPs, is Internet Explorer.

237. Although both Microsoft and Netscape's products recently have received favorable and comparable reviews, one influential reviewer, CNet, reversed its review in favor of Internet Explorer and chose Navigator 4.0, citing security and stability problems with Internet Explorer 4.0. ("Battle of the Sumo Browsers," CNet, by Rex Baldazo, 9/29/97, updated 10/17/97; updated 2/18/98 and 4/2/98 by Cormac Foster.). Indeed, even Microsoft's Steve Ballmer acknowledged that significant quality issues have been raised about Internet Explorer 4.0. ("Ballmer: IE4.0, A Trade Off," CNet, December 5, 1997).

238. Microsoft publicly has claimed that Internet Explorer 4.0 won 19 out of 20 head-to-head reviews against Navigator. Because I was generally familiar with the reviews at the time that Microsoft made this statement and, based on my knowledge of those reviews, believed it to be false, I commissioned

some research to be done regarding the veracity of Microsoft's contention. The researcher did not even find 20 reviews in which the products were reviewed head-to-head. Of the handful of reviews that did look at the products head-to-head, the results were a mixed bag. Some reviewers preferred certain features of Internet Explorer over Navigator and some preferred certain features of Navigator over Internet Explorer.

239. Microsoft also has suggested that Netscape's loss of market share is due to its own "bad" corporate decisions. Sure, I agree we may have made some decisions that in hindsight I might not have made, but so has every company, including Microsoft. Indeed, when the Internet revolution began -- a revolution based on open standards and open access to all -- Microsoft was spending hundreds of millions of dollars developing and marketing its proprietary on-line service called the Microsoft Network ("MSN"). MSN, by all accounts, did not succeed, and Microsoft was forced to play catch-up in the already exploding Internet marketplace. In a competitive market, a company frequently can recover even from a major strategic mistake, like Microsoft's. However, in a market being targeted by a monopolist, such as Microsoft, even a routine misstep can be devastating. Moreover, no matter how a competitor attempts to adjust to the monopolist's predatory practices, those practices clearly will have a detrimental effect. Indeed, they did. No matter how Netscape adjusted, we ultimately had to abandon our business model, forego

all browser revenue, and formulate and implement a new business model in a short period of time. This has been a difficult mission. Even now, with Netscape's new business model, Netscape is getting reports of Microsoft targeting its new business plans. Indeed, as recently as September 21, 1998, Netscape learned that a European Internet Content Provider could not post a Netscape downloading button because the Content Provider was prohibited from doing so by its contractual obligations to Microsoft. Moreover, even after Netscape began giving its browser away for free in early 1998, Netscape continues to lose market share to Microsoft. This poses a problem for Netscape because, even though it has shifted its business strategies, our browser is important to continued brand recognition and constitutes a significant avenue for distribution and promotion of other Netscape products and other important technologies, such as Java.

NETSCAPE'S BUSINESS GOING FORWARD

240. Despite, and in response to, Microsoft's anticompetitive practices, Netscape's business strategies have continued to evolve. Netscape is a public company, and as such our shareholders expect us to analyze the market and move forward to do our best to produce a positive return on their investments. We cannot, and have not, closed up shop and gone home in the face of Microsoft's unrelenting attack on our browser business.

241. The market reality today is that browsers are free. Netscape generates no

income from the browser we continue to ship. In this regard, we have studied the market and have proceeded to enter new businesses.

242. Because Netscape's employees are among the most knowledgeable in the world about the Internet, and because we have continued to recruit new talent aggressively, the knowledge base of the Netscape work force and their innate ability and desire to continue innovating in the Internet software space are Netscape's greatest assets. This has allowed Netscape to enter and succeed dramatically in two new emerging markets.

243. For example, today, Netscape generates more total revenue -- largely from Enterprise Internet Software and Internet portals -- than it did when the browser still generated revenue.

244. In the Enterprise Internet Software space, Netscape has become a leader in: (1) messaging systems for electronic mail; (2) application servers which enable businesses to build custom Internet applications for their employees, partners and customers, and Internet directory and system management software; (3) web publishing applications; and (4) electronic commerce applications. Our customers include many of the largest and most important corporations in the world who have placed their trust in our ability to continue to innovate, to produce quality software, and to deliver superior service and support.

245. In addition, Netscape is also one of the leading Internet Portal companies.

Today, Netscape Netcenter has over 7 million registered users and is consistently one of the five most visited websites on the Internet as measured by independent sources. Users visit Netcenter to access: (1) several leading Internet search engines; (2) web-based electronic mail; (3) software downloads for dozens of applications made by Netscape as well as many other software vendors; (4) personalized news and information; and (5) other content and communications.

246. The future of Netcenter represents nothing short of a fundamental shift in the way most people will access news, financial and banking services, employment services, and communication resources. The most recently announced innovations include the convergence of Netcenter and online banking, as well as Netcenter and telephone, paging and fax services. Today, people surf the web and visit portals primarily to access static information sources. Tomorrow, through continued Netscape innovations and partnerships with the world's leading enterprises, people will use Netcenter to manage their finances, pay bills, and make phone calls.

247. Netscape will also continue the convergence of Netcenter and the enterprise software business. While some of the world's largest companies have been among the earliest adopters of Enterprise Internet Software, it is clear that smaller businesses must also adopt these technologies in order to remain competitive. Netcenter will provide an affordable opportunity for small

businesses to avail themselves of these technologies so they can interact with their geographically dispersed, and in many cases much larger, trading partners. Businesses will have the opportunity to increase dramatically their profitability and productivity through the use of these and other future Netscape innovations.

REMEDY

248. I have been asked by many people what I believe would be an appropriate and effective remedy for Microsoft's anti-competitive conduct, described above. While that decision, of course, is not for me to make, I believe the most important factor the Court should consider is the remedy's effects on competition and consumers.

249. The browser is important not simply to Netscape, but because, as Bill Gates explicitly recognized, it offers the opportunity for an alternative software platform and a paradigm shift in the industry. This could have a major effect on competition and consumers. I do not believe in government regulation of the software industry, so I do not believe it is up to the government to decide whether such a development would be good or bad. Rather, I believe that consumer choice in a free market leads to more innovation and ultimately to the products and approaches consumers want most at the lowest possible price.

250. Unfortunately, due to Microsoft's use of its monopoly power over the

operating system to squelch competition in the browser market, consumers for the last three years have not had an unfettered choice. Any remedy, to be effective, must prevent the use of such monopoly power to stifle innovation and choice. One way to do that, of course, would be to separate Microsoft's operating system efforts and personnel from those working on applications software, so that competition in the latter area would not be unfairly limited by the power of the monopoly operating system. I believe that the most appropriate remedy for the practices I have described above would be to order Microsoft to distribute Internet Explorer separately from its operating system products and to be prohibited from forcing the "bundling" of those two products or from entering into exclusionary contracts relating to distribution of Internet Explorer. In particular, one of the consumer advantages that Microsoft uses to argue in favor of its so-called "integration" is the ability of its browser to browse information located on distant sites (such as the Internet) and on local sites (such as a computer's hard drive) in a consistent fashion. This, however, as well as a host of other advantages that Microsoft claims to have achieved by "integration," does not justify "integration" by Microsoft, because the Netscape product, or a competing browser, is capable of accomplishing the same tasks with the same benefits when installed on Windows.

251. In the final analysis, whatever precise approach the Court adopts, I believe

the touchstone should be to give consumers a full, fair choice of products, without the power of a monopoly operating system pushing them in a direction that free competition may or may not achieve. Only such free competition will result ultimately in innovation and the best products at the lowest prices.

I declare under penalty of perjury of the laws of the United States that the foregoing is true and correct.

Executed this 13th day of October 1998 at Mountain View, California.

James Barksdale,
President & CEO
Netscape Communications Corporation