UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF COLUMBIA

STATE OF NEW YORK *et al.*, Plaintiffs, - against – MICROSOFT CORPORATION, Defendant.	Civil Action 98-1233 (CKK)

PLAINTIFF STATES' MOTION TO EXTEND THE MODIFIED FINAL JUDGMENT UNTIL NOVEMBER 12, 2012

Plaintiff States California, Connecticut, Iowa, Kansas, Minnesota, the Commonwealth of Massachusetts and the District of Columbia (Movants), pursuant to § VII of the Modified Final Judgment and Rule 60(b) of the Rules of Civil Procedure, respectfully move the Court to extend expiration of all provisions of the Modified Final Judgment, except § III.B, until November 12, 2012 for the following reasons, and as more fully set forth in the Memorandum of Points and Authorities and associated expert reports, attached and incorporated by reference herein:

A. An additional three year extension of § III.E. to November 12, 2012 is warranted because of continuing problems with the implementation of § III.E., particularly the availability of Communications Protocols (CPs) that should have been documented in Microsoft's initial implementation efforts in 2001. The recent Icon/Nicholson report concluded that there were four major flaws in the design and execution of Microsoft's effort to identify all the CPs that should have been disclosed such that Icon/Nicholson could not say with confidence that all necessary CPs had been disclosed. The continuing problems with the Microsoft

Communications Protocol Program (MCPP) justify government oversight throughout the life of the MCPP. Extension of § III.E now will also provide current and potential industry recipients of the Technical Documentation (TD) with greater confidence that all required CPs are disclosed and described accurately.

B. The competitive benefits to be derived from servers implementing the CPs are in many instances dependent upon the middleware-related provisions found at §§ III.A., III.C., III.D. III.F.2, III.G., and III.H. of the Modified Final Judgment. Given that Microsoft is just now delivering complete TD - after years of delay during which it increased its share of the server market - it would be unreasonable to terminate the middleware-related provisions now because § III.E. would then effectively operate in a vacuum.

C. In particular, § III.H. of the Modified Final Judgment has yet to pry open the OEM channel of distribution to competitive browsers, because no major OEM currently distributes a browser other than Microsoft's Internet Explorer (IE). Many new middleware technologies are just now appearing that may, in the near future, pose a competitive threat to Microsoft's operating system monopoly. These technologies substantially depend upon the browser. Because Microsoft still retains control of the OEM channel for browser distribution, in part because its illegal conduct with respect to IE has not yet been fully remedied, it is critical that §§ III.A., III.C., III.D. III.F.2, III.G., and III.H. of the Modified Final Judgment be continued until these technologies mature.

Consequently, Movants respectfully request that the Court issue an order:

1) Modifying § V.A. of the Modified Final Judgment to extend the expiration of all provisions of the Modified Final Judgment, except § III.B., until November 12, 2012;

2) Vacating § III.B in its entirety;

3) Vacating the initial parenthetical sentence of § III.F.1 of the Modified Final Judgment, so as to continue § III.F.1 until November 12, 2012; and

4) Directing such additional relief as is necessary and appropriate.

A proposed order and proposed Second Modified Final Judgment are attached hereto for the Court's consideration.

Dated: October 16, 2007

Respectfully submitted,

FOR THE STATES OF CALIFORNIA. CONNECTICUT, IOWA, KANSAS, MASSACHUSETTS, MINNESOTA AND THE DISTRICT OF COLUMBIA

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UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF COLUMBIA

STATE OF NEW YORK *et al.*, Plaintiffs, v. MICROSOFT CORPORATION, Defendant.	Civil Action 98-1233 (CKK) Next Court Deadline: November 6, 2007 Status Conference

PLAINTIFF STATES' MEMORANDUM OF POINTS AND AUTHORITIES
IN SUPPORT OF THEIR MOTION TO EXTEND
THE FINAL JUDGMENT THROUGH NOVEMBER 12, 2012

Plaintiff States California, Connecticut, Iowa, Kansas, Minnesota, the Commonwealth of Massachusetts and the District of Columbia respectfully submit this memorandum in support of their motion, made pursuant to §VII of the Final Judgment and Rule 60(b) of the Rules of Civil Procedure, to extend all provisions of the Modified Final Judgment, except § III.B, through November 12, 2012.

INTRODUCTION

As the Court of Appeals has stated, "the key to the proper remedy in this case is to end Microsoft's restrictions on potentially threatening middleware, prevent it from hampering similar nascent threats in the future, and restore competitive conditions created by similar middleware threats." *Massachusetts v. Microsoft Corp.*, 373 F.3d 1199, 1243 (D.C. Cir. 2004) (quoting United States Response to Public Comments ¶ 17).

In fact, it is only recently that such "similar nascent threats" – what Microsoft's experts refer to as "new" or "emerging" products and services – have begun to appear.[1] Accordingly, the protections afforded to middleware by the Final Judgment are more necessary now than ever and should not be allowed to lapse precisely when they could be most useful in achieving the objectives enumerated by the Court of Appeals. Extension of the Final Judgment is especially critical since many of the most promising "new" and "emerging" technologies, like Internet-centric or web-based applications, are accessed by consumers through products over which Microsoft retains tight control because of its enduring monopoly power – PC operating systems (more than 90% market share) and web browsers (more than 80% market share).

Microsoft has delayed for almost five years discharging the principal affirmative obligation required of it by the Final Judgment - providing the complete and accurate Technical Documentation (TD) necessary to implement §III.E. The last milestone of the rewritten TD (M5+90) was finally delivered by Microsoft only a few weeks ago and is still subject to extensive analysis and testing by the Technical Committee (TC).[2]

Microsoft's failure to supply adequate TD in a timely manner has undermined the Court's expectation that §III.E would assist in facilitating interoperability between Windows and third-party software:

> [T]he goal of facilitating interoperation between Microsoft's PC operating system products and third-party middleware, as well as between Microsoft's PC operating system products and third-party server operating systems, is consistent

[1] *See generally* Expert Reports of Marco Iansiti, dated August 29, 2007 ("Iansiti Rep.") and of David S. Evans and Albert L. Nichols, dated August 30, 2007 ("Evans/Nichols Rep."), both of which are appended to Microsoft's Report Concerning the Final Judgments, dated August 30, 2007.

[2] Even though Microsoft initially delivered milestone M5+90 as scheduled, M5+90 did not include the XML markup used by the TC for testing - because Microsoft used an outdated version of the TC's validation tool – and Microsoft has to test the M5+90 XML markup again. Microsoft Supp. Status Report, filed October 15, 2007, at 1-2; *see also* Joint Status Report, filed August 31, 2007, at 8-9.

> with the goal of "ensur[ing] that there remain no practices likely to result in monopolization in the future." *United Shoe*, 891 U.S. at 250, 88 S.Ct. 1496.

New York v. Microsoft Corp., 224 F. Supp. 2d 76, 171 (D.D.C. 2002). While Microsoft has defaulted on its §III.E obligations, it has consolidated its hold on the server market where its share of shipments has increased from 55% in 2002 to 73% in 2006. Report of John E. Kwoka, Jr., dated October 16, 2007, annexed to plaintiffs' motion as Exhibit A ("Kwoka Rep."), App. 2, Exh. 4. In this respect at least, not only have the "competitive conditions created by similar middleware threats" not been "restored," but they have deteriorated.

As the Court of Appeals also recognized, an important purpose of this Court's remedy was to "deny to the defendant the fruits of its statutory violation." *Massachusetts v. Microsoft, supra,* 373 F.3d at 1232. Microsoft's "freedom from the possibility rival middleware vendors would pose a threat to its monopoly" was identified by the Court of Appeals as the "fruit of its violation." *Id.*, at 1233. The Court of Appeals also confirmed that this Court, therefore, had correctly "identified opening the channels of distribution for rival middleware as an appropriate goal for its remedy" and noted approvingly that "by pry[ing] open these channels, [Citation], the district court denied Microsoft the ability again to limit a nascent threat to its operating system monopoly." *Id.*

At the most recent Status Conference, the Court observed that a request to extend the Final Judgment should be "for an identifiable purpose." Tr., No. 98-1233 (CKK), September 11, 2007, at 36. We respectfully submit that, for the reasons discussed below, the requested extension is necessary to give the Final Judgment an opportunity to achieve the objectives that were endorsed by the Court of Appeals but have not yet been realized: to prevent Microsoft from using its enduring monopoly power to hamper nascent

platform threats, to restore competitive conditions created by platform threats similar to those posed by Netscape and Java, and to deny Microsoft the fruits of its statutory violation.

SUMMARY OF FACTS

A. PC Operating Systems

The market for PC operating systems over the past fifteen years has been characterized by Microsoft's enduring monopoly and its slow pace of product introduction. Kwoka Rep., at ¶¶ 8, 44. Microsoft's share of the PC operating system market has been greater than 90% for at least the past 15 years. *Id.*, at ¶ 8, 35. Microsoft's monopoly of the PC operating system market is protected by strong network effects and the applications barrier to entry. *Id*., at ¶ 8. Since the Final Judgment was entered in November, 2002, Microsoft has introduced only one new version of Windows – Vista in January, 2007. Report of Ronald S. Alepin, dated October 16, 2007, annexed to plaintiffs' motion as Exhibit B ("Alepin Rep."), at ¶ 24, App. 3. In contrast, from August 1995 until October 2001, Microsoft distributed five distinct operating systems (Windows 95, 98, Me, 2000 and XP). *Id.*.

B. Web Browsers

Microsoft's Internet Explorer (IE) is the dominant browser with a usage share of approximately 80%. Since the Final Judgment was entered, Microsoft has introduced only one major version of IE – IE 7 on October 18, 2006. Alepin Rep., at ¶¶ 24 & 26, App. 3. In contrast, from August 1995 until March 2001, Microsoft distributed eight major versions of IE (versions 1.0, 2.0, 3.0, 4.0, 4.5, 5.0, 5.5 and 6) for several versions

of Windows and other operating systems (e.g., IE 4.5 for Macintosh and IE 4.0 for Solaris). Alepin Rep., at ¶ 24, App. 3. No major OEM currently preloads a browser other than IE on its new PC systems. Alepin Rep., at ¶ 41; *see also* Evans/Nichols Rep., at 6, Table 3 (no non-Microsoft browser installed on surveyed machines).

The Firefox browser, developed by the not-for-profit Mozilla Foundation, has the second largest usage share of any other browser – approximately 15%. It must be downloaded by consumers because it is not preinstalled by any major OEM. *Id.* Despite glowing critical reviews for its innovative features, Firefox's usage share has apparently stalled at 15%, possibly due to users' reluctance to download and install new software. See, e.g., Alepin Rep., at ¶ 41, n.77. OEM preinstallation remains an important distribution channel for browsers today. Alepin Rep., at ¶¶ 88-96.

The browser also remains an important product today because it is used to access such new and emerging technologies as web-based applications. *Id.* at 28 & 29. Some of these technologies may eventually develop into platform threats to Microsoft's Windows monopoly. Microsoft, however, has the ability - by virtue of IE's dominance and its resulting control of web standards - to use the browser as a chokepoint with respect to consumer access to the Internet-centric technologies that currently represent the most promising nascent platform threats to Windows. *Id.* at ¶ 29.

C. Nascent Platform Threats

Potential platform threats to Microsoft's dominance in the PC operating system market are just beginning to emerge. The most significant of these threats are web-based technologies that open the markets to competition by reducing the "applications barrier to entry." Sometimes referred to as "Web 2.0", these technologies are very early along the

"hype cycle," meaning that they have not reached the level of maturity necessary for mainstream adoption.[3] Alepin Rep., at ¶ 79, Fig. 1. Like other software, web-based applications require computer equipment running a client or server operating system. Microsoft remains the dominant supplier for these operating systems. Microsoft's share of the PC operating system market has remained higher than 90% for at least 15 years and its share of server shipments has increased from 44% in 2000 to 73% in 2006.

Additionally, to reduce the applications barrier to entry, web-based platform threats require a web browser that is compliant with industry standards. *E.g.*, *see* Alepin Rep., at ¶¶ 38 & 44. The web-based platform threats are currently dependent on Microsoft's compliance with industry standards because its IE browser has an approximately 80% usage share. Until the web-based platform threats erode the applications barrier to entry, these platform threats remain vulnerable to Microsoft's control of the browser and the operating system. Market research estimates that web-based applications will not reach parity with Windows-specific applications until at least 2011. Alepin Rep., at ¶ 20; *see also* Iansiti Rep. at 62, n.96.

D. MCPP

The Microsoft Communications Protocol Program (MCPP) was created by Microsoft to fulfill its §III.E disclosure obligations. Microsoft knew that it would be required to produce the TD at least as early as November 2001, when it entered into the Consent Decree with the settling plaintiffs.[4] Microsoft's obligation to make the TD

[3] According to Gartner, the emerging technology "hype cycle" can take 2-10 years (or more) until new technology is considered mature, and consists of: 1) Technology Trigger; 2) Peak of Inflated Expectations; 3) Trough of Disillusionment; 4) Slope of Enlightenment; and finally 5) Plateau of Productivity. Alepin Rep. at ¶ 79, Fig. 1 (Gartner Emerging Technologies Hype Cycle, 2005).

[4] Stipulation ("Revised Proposed Final Judgment"), dated November 6, 2001 (No. 98-1233), *available at* http://www.usdoj.gov/atr/cases/f9400/9495.pdf

available commenced on February 1, 2003, three months after the Final Judgment was entered. The TD initially produced by Microsoft was characterized by an increasing number of "bugs" identified by the TC. Microsoft finally proposed a "reset" of the TD – *i.e.*, TD written from scratch from the "bottom up" – which was approved by the Court in May, 2006. The fifth and final milestone of the rewritten TD was provided to the TC on or about September 28, 2007. Microsoft Supp. Status Report, filed October 15, 2007, at 1-2.

As of August, 2007 there were 29 MCPP licensees, of which only 13 had shipped product under their licenses. Nine of these 13 companies described their products as being primarily complements to Windows servers. No licensee has built a general server using its license. California Group's Report on Remedial Effectiveness, filed August 30, 2007, at 8 & 11, Exh. 5.

ARGUMENT

I. THE COURT HAS BROAD DISCRETION TO MODIFY THE FINAL JUDGMENT TO ACCOMPLISH ITS INTENDED RESULT

The power of a court in equity to modify a decree of injunctive relief is long-established, broad, and flexible. *New York State Ass'n for Retarded Children, Inc. v. Carey*, 706 F.2d 956, 967 (2d Cir. 1983), *cert. denied*, 464 U.S. 915 (1983). At the request of the party seeking equitable relief, the court is granted broad discretion to modify a decree in order to accomplish its intended result. *See United States v. United Shoe Mach. Corp.*, 391 U.S. 244, 251-252, 20 L.Ed 2d 562, 88 S.Ct 1496 (1968); *United States v. Western Elec. Co., Inc.*, 46 F.3d 1198, 1202 (D.C. Cir. 1995). As the Court of Appeals stated in this case, "a district court is afforded broad discretion to enter that relief

it calculates will best remedy the conduct it has found to be unlawful." *United States v. Microsoft Corp.*, 253 F.3d 34, 105 (D.C. Cir. 2001). This is particularly true for antitrust cases, where a district court "is clothed with 'large discretion' to fit the decree to the special needs of the individual case." *Id.* (quoting *Ford Motor Co. v. United States*, 405 U.S. 562, 573 (1972)). Section VII of the Final Judgment, which restates the applicable law, provides that any party can "apply to this Court at any time for further orders and directions as may be necessary or appropriate to carry out or construe this Final Judgment, [or] to modify or terminate any of its provisions…."[5]

The modifications requested herein are necessary to ensure that the Final Judgment does in fact accomplish its intended result – *i.e.*, that it "be effective 'to redress the violations' and 'to restore competition.'" *Ford Motor Co. v. United States*, 405 U.S. 562, 573 (1972) (quoting *United States v. E. I. Du Pont De Nemours & Co.*, 366 U.S. 316, 326 (1961)). To be successful, a remedy in an antitrust case must "cure the ill effects of the illegal conduct, and assure the public freedom from its continuance," *id.* at 573 n.8 (quoting *United States v. United States Gypsum Co.*, 340 U.S. 76, 88 (1950)), as well as "effectively pry open to competition a market that has been closed by [a] defendant['s] illegal restraints." *Id.* at 577-588. The standard of review for modifications made pursuant to the Court's express retention of authority to modify a judgment is abuse of discretion. *United States v. Western Elec.*, 894 F.2d 430, 435 (D.C. Cir. 1990) (citing

[5] The Final Judgment also provides, at § V.B, that "[i]n any enforcement proceeding in which the Court has found that Microsoft has engaged in a pattern of willful and systematic violations, the Plaintiffs may apply to the Court for a one-time extension of this Final Judgment of up to two years…." Section V.B was imported into the Final Judgment from the United States case and, as the United States made clear during the Tunney Act proceedings, "[t]his provision is designed to supplement the government's traditional authority to bring contempt actions." Competitive Impact Statement, November 15, 2001, at §IV.C (No. 98-1233), *available at* http://www.usdoj.gov/atr/cases/f9500/9549.pdf. At the September 11, 2007 Status Conference, the Court recognized this distinction, observing "that the assessment in general involves different considerations when you're reviewing compliance issues as opposed to the effectiveness of the various provisions of the final judgment…." Tr., No. 98-1233 (CKK), September 11, 2007, at 32.

System Fed'n No. 91, Ry. Employees' Dep't, AFL-CIO v. Wright, 364 U.S. 642, 647-48, 5 L. Ed. 2d 349, 81 S. Ct. 368 (1961); *Envtl. Def. Fund, Inc. v. Costle*, 636 F.2d 1229, 1250 (D.C. Cir. 1980).

II. SECTION III.E. OF THE FINAL JUDGMENT SHOULD BE EXTENDED THROUGH NOVEMBER 12, 2012

Section III.E. of the Final Judgment provides, in relevant part: "Starting three months after the entry of this Final Judgment, Microsoft shall make available for use by third parties for the sole purpose of interoperating or communicating with a Windows Operating System Product [certain Communications Protocols] …." This is not a requirement that was imposed by the Court on Microsoft over its objection. Rather, it was an obligation voluntarily assumed by Microsoft as an inducement to the settling plaintiffs to terminate this litigation. Microsoft, which was aware of its obligation in this regard well before the Final Judgment was entered, established the MCPP as the vehicle through which it would provide TD to disclose the required information about the covered Communications Protocols (CPs).

As the Court is aware, the MCPP has been fraught with problems since its inception. Only after the TC had identified increasingly large numbers of "bugs" in the TD did Microsoft finally concede the serious nature of the problems. In the spring of 2006, Microsoft proposed a "reset" - i.e. a complete rewriting of the TD. At the Status Conference on May 17, 2006, when the Court approved the "reset," Microsoft acknowledged that the then existing version of the TD "wasn't really meeting the needs

of anyone, and in fact the way we were thinking about the problem was incorrect."[6] In conjunction with the "reset," Microsoft consented to an extension of §III.E and the other provisions of the Final Judgment necessary to effectuate it for an additional two years, until November 12, 2009.[7]

Notwithstanding the "reset," problems continue with the TD. Although the rewritten TD appears to be improved, the last three Joint Status Reports provide the following count of Technical Document Issues (TDIs) in the rewritten documentation, as of the dates indicated:

183 TDIs	2/28/07
182 TDIs	5/31/07
711 TDIs	7/31/07

As of September 30, 2007, Microsoft reports an increase of TDIs to 723. Microsoft's Supp. Status Report, filed October 15, 2007, at 4. More significantly, there are continuing questions not just about the accuracy of the TD, but whether the TD is complete – i.e. whether Microsoft has disclosed all the CPs it is required to disclose to ensure the interoperation mandated by §III.E. In the Joint Status Report, dated March 6, 2007, plaintiffs reported their concern that Microsoft was still "discovering" CPs that should have been documented long ago. In their next Joint Status Report, dated June 19, 2007, plaintiffs informed the Court that the TC planned to hire an independent auditor to conduct an "audit" of Microsoft's project (code-named "Project Sydney") that supposedly had identified all the CPs it was required to disclose.

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[6] Tr., No. 98-1233 (CKK), May 17, 2006, at 56. Microsoft ascribed its problems with producing better TD to the fact that it "didn't have the exact right resources…[or]the right process in place." *Id.* at 39.

[7] In addition, Microsoft informed the Court that it would make current MCPP protocols "and future Windows client/server protocols" available for license through November 11, 2012. Joint Status Report on Microsoft's Compliance with the Final Judgments, dated May 12, 2006 (No. 98-1233), at 11 n.9, *available at* http://www.usdoj.gov/atr/cases/f216100/216127.pdf.

The independent audit took place between July 25 and August 24, 2007, and the report of the auditor (Icon/Nicholson) was provided to plaintiffs on August 29.[8] As the California Group advised the Court at the September 11, 2007 Status Conference, Icon/Nicholson identified what the auditors called four major flaws in the design and execution of Microsoft's effort to identify all the communications protocols that should have been disclosed. Icon/Nicholson concluded that they could not say with confidence that all necessary communications protocols have been disclosed. Tr., No. 98-1233 (CKK), September 11, 2007, at 27-28; *see also* Tr., No. 98-1233 (CKK), October 16, 2007 .

There is one constant verity about the MCPP – whatever Microsoft has promised to do to correct problems has taken more time and more resources than it had forecast. There is no reason to expect that the effort to rectify the problems identified by the Audit will be any different. Moreover, the set of protocols that must be documented continues to change as the communications between the Windows client and the yet-to-be-released Windows Server 2008 are finalized. In addition, because present and future client/server CPs are available for license through November 11, 2012, Microsoft will be required to document any such new CPs in its next major Windows client and server releases. Microsoft has announced that Windows Server 2008 will be launched on Feb. 27, 2008, and the next major version of the Windows client (currently named "Windows 7") is tentatively scheduled to be shipped in approximately three years (i.e., 2010). Alepin Rep., at ¶ 24. It is imperative that the TC be available to analyze and test TD written by

[8] At a telephonic Court conference on October 16, 2007, the moving plaintiffs indicated that they intended to file a copy of the Icon/Nicholson report, under seal, with this motion. After discussions with the Court and all parties, the moving plaintiffs are not doing so, but reserve all rights to file the Icon/Nicholson report in support of this motion at a later time, pursuant to order of the Court. *See* Tr., No. 98-1233 (CKK), October 16, 2007.

Microsoft for any new covered CPs to make certain that it is complete and accurate. Given the troubled history of the MCPP, the as yet unresolved problems with the rewritten TD, and Microsoft's obligation to disclose and document any additional CPs incorporated into its new products, there can be little doubt that continued oversight by plaintiffs, the TC, and the Court, is essential to assure the integrity of the MCPP.

Oversight is required not merely to assure the Court and plaintiffs that Microsoft fulfills its §III.E disclosure obligations.[9] Even more importantly, the assurance of continuing oversight is necessary to give prospective licensees confidence that the TD they will get, if they take a license, is accurate and complete. At this point in time, it is neither reasonable nor fair to expect a company considering a license to proceed without such assurance. That is especially true of companies that might use a license to build a general server, which requires considerable advance planning, capital investment and other expenditure. It is precisely those types of licensees that the MCPP must attract to realize the remedial objectives of the Final Judgment.[10]

The MCPP may yet be able to attract those types of licensees, especially if they are reassured that oversight by the plaintiffs and the TC - and ultimately by the Court – will continue for the five additional years Microsoft has committed to licensing the TD. The MCPP's potential attractiveness was undoubtedly enhanced by the very significant decision rendered last month by the Court of First Instance, rejecting Microsoft's effort to

[9] The Court repeatedly has asked plaintiffs why Microsoft has failed to discharge its §III.E obligations. The moving plaintiff states profess continuing puzzlement why a corporation with Microsoft's monetary and human resources has still not been able to deliver on a promise it made to the settling plaintiffs and the Court more than five years ago. What can be said with certainty, however, is that without continual prodding from the plaintiffs and the TC and the possibility that it may be found in contempt, Microsoft has no incentive to produce TD that may enable its competitors to compete more vigorously against it.

[10] As the California Group reported to the Court, based on its recent licensee survey, nine of the 13 companies that actually had shipped products pursuant to their MCPP licenses described their products as being complements to Windows servers, and none has used its MCPP license to produce a general server product. California Group's Report on Remedial Effectiveness, dated August 30, 2002, at 8.

overturn the European equivalent of MCPP, the Work Group Server Protocol Program (WSPP).[11] WSPP, unlike MCPP, includes server-to-server protocols and is more susceptible of use by providers of open source products that now constitute Microsoft's principal competition in the server market. As the California Group plaintiffs informed the Court at the September 11 Status Conference, they intend to work to harmonize MCPP with WSPP to make the combined programs as attractive as possible to prospective licensees who might build products that actually compete with, rather than just complement, the Windows platform. Tr., No. 98-1233 (CKK), September 11, 2007, at 43-45.

The Final Judgment contemplated that oversight by plaintiffs and the TC would run simultaneously with the CP disclosures mandated by §III.E. Given Microsoft's failure to produce adequate TD in the past five years, its significantly enhanced presence in the server market during the same period of time, and the renewed vitality of WSPP, there is more reason than ever to make certain that - as the Court originally intended - oversight runs concurrently with the period of time the TD is available for licensing.

III. THE OTHER MIDDLEWARE-RELATED PROVISIONS OF THE FINAL JUDGMENT SHOULD ALSO BE EXTENDED THROUGH NOVEMBER 12, 2012

A. Section III is a carefully crafted unitary framework that cannot be disaggregated if it is to succeed in depriving Microsoft of the "fruits of its violation"

The middleware-related subparagraphs of §III were intended to operate together, in a carefully constructed unitary framework, to foster the development and distribution

[11] *See* http://curia.europa.eu/jurisp/cgi-bin/gettext.pl?lang=en&num=79929082T19040201&doc=T&ouvert=T&seance=ARRET ("Judgment of the Court of First Instance").

of nascent platform threats. It assuredly was never contemplated that any subparagraph of §III – including subparagraph E – could alone succeed in nurturing nascent middleware threats – the ultimate remedial objective of the Court of Appeals - in an environment dominated by Microsoft's entrenched monopoly.[12]

In its Memorandum in Support of the Entry of the Proposed Final Judgment, dated February 27, 2002, the United States stressed that "the RPFJ's effectiveness would be undercut unless it addressed the rapidly growing server segment of the market" (at 59) and that it had "carefully crafted the RPFJ to address the conduct found unlawful by the Court of Appeals" (at 62).[13] The United States relied extensively on the supporting Declaration of its economist Dr. David B. Sibley, annexed to its Memorandum as Exhibit C. Dr. Sibley underscored the interconnected nature of the various subparagraphs of Section III (at ¶52):

> [T]he SRPFJ's focus is on restoring the competitive threat provided by middleware…. This is accomplished by providing middleware developers the means to create competitive products through: (1) provisions for API disclosure; (2) provisions that require Microsoft to create and preserve default settings, such that Microsoft's integrated middleware functions will not be able to over-ride the selection of third-party middleware; (3) the creation of "add/delete" functionality that make it easier for OEMs and end-users to replace Microsoft middleware functionality with independently developed middleware; and (4) requirements for Microsoft to license communications protocols embedded in the OS while maintaining Microsoft's ability to deploy proprietary technology provided separately….

The logic of this approach is self-evident. Nascent platform threats cannot realize their potential unless they can be delivered in various ways to the Windows desktop – including directly on new PC systems and indirectly from third party servers via the

[12] We have not requested the continuation of §III.B, which relates to uniform terms and conditions on the sale of Windows to OEMs, and its discontinuance will remove a not insubstantial administrative burden on Microsoft.

[13] *Available at* http://www.usdoj.gov/atr/cases/f10100/10143.pdf.

browser. Indeed, §III's multifaceted approach, which protects a variety of distribution channels, mirrors Microsoft's anticompetitive tactics, which were intended to foreclose a variety of means used by Netscape/Java to reach consumers. As the Court of Appeals noted, "Microsoft undertook a number of anticompetitive actions that seriously reduced the distribution of Navigator, and the District Court found that those actions thereby seriously impeded distribution of Sun's JVM." *United States v. Microsoft Corp.*, *supra*, 253 F. 3d at 75-76.[14]

Just as Microsoft sought to impede the distribution of rival products in various ways, so too did the settling plaintiffs – and the Court – seek to "pry open" a variety of distribution channels to allow rival products to reach the Windows desktop, in addition to prohibiting Microsoft from resuming the specific anticompetitive acts condemned by the Court of Appeals. Thus, for example, it would make little sense to require Microsoft to license client-to-server CPs which make rival middleware accessible from third-party servers (§III.E) if Microsoft were free to retaliate against OEMs, ISVs and IHVs for distributing that middleware (§§III.A and F), to prevent OEMs from promoting that middleware (§§III.C and H), to conceal APIs necessary to enable that middleware to interoperate with Windows (§III.D), and to induce software companies not to distribute that middleware (§III.G).

[14] In its decision, the Court of Appeals described a multiplicity of methods Microsoft used to impede the distribution and development of Netscape/Java, including exclusive deals with IAPs ("Microsoft's deals with the IAPs clearly have a significant effect in preserving its monopoly; they help keep usage of Navigator below the critical level necessary for Navigator or any other rival to pose a real threat to Microsoft's monopoly" *id.* at 71); First Wave Agreements with ISVs ("Microsoft's deals with major ISVs had a significant effect upon JVM promotion" *id.* at 75); threats to Intel ("Microsoft's internal documents and deposition testimony confirm both the anticompetitive effect and intent of its actions" *id*. at 77); and an exclusive browser distribution deal forced upon Apple ("Because Microsoft's exclusive contract with Apple has a substantial effect in restricting distribution of rival browsers, and because (as we have described several times above), reducing usage share of rival browsers serves to protect Microsoft's monopoly, its deal with Apple must be regarded as anticompetitive" *id.* at 73-74).
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Moreover, to "unbundle" the Court's remedy, by allowing only §III.E to continue in isolation, would reward Microsoft for its failure to satisfy its disclosure obligations in a timely manner. Microsoft's conduct – whether willful or negligent – has precluded the Final Judgment from functioning as a whole, as was clearly intended, for the past five years. Unless all the middleware-related provisions of the Final Judgment are allowed to function together over a consecutive five-year period, supporting and reinforcing each other, Microsoft will have succeeded in emasculating the core portion of the remedy designed to deprive it of the "fruits of its violation." *See also* Alepin Rep., at ¶ 10.

B. Competitive conditions have not been restored because critical distribution channels for rival middleware have not yet been pried open

The prying open of key distribution channels for software that poses a potential platform threat to Windows was clearly one of the principal remedial objectives endorsed by the Court of Appeals. *See, e.g, Massachusetts v. Microsoft, supra*, 373 F.3d at 1232-33. As discussed above, however, Microsoft has substantially increased its presence in the server market while defaulting on its §III.E disclosure obligations. Since the Final Judgment was entered, therefore, the potential of non-Microsoft servers to provide an alternative platform for delivery of rival middleware - which §III.E was intended to foster - has deteriorated.

Likewise, the situation has deteriorated with respect to OEMs' preinstallation of third-party browsers. The browser, of course, is historically important because it was the nascent platform threat at which most of Microsoft's anticompetitive conduct established at the trial was directed. The browser remains just as important today because it is the link between the Windows desktop and the "emerging" web-based and Internet-centric applications that Microsoft's experts have identified as potential platform threats to

Windows.

As the Court of Appeals affirmed, Microsoft's commingling of browser and operating system code and exclusion of IE from the Add/Remove Programs utility, which deterred OEMs from installing a second browser by increasing their product testing and support costs, violated §2 of the Sherman Act . *United States v. Microsoft, supra*, 253 F3d. at 64-67. Subsequently, the Court of Appeals upheld the sufficiency of the "hide access" remedy for this violation, on the theory that it would enable OEMs "to avoid the costs of having to support both IE and a rival web browser" and would make OEMs "more likely to install a rival browser based upon market determinants like consumer demand." *Massachusetts v. Microsoft, supra*, 373 F.3d at 1238-39.

In fact, the expectation of the Court of Appeals has not yet been realized with regard to OEMs' preinstallation of browsers, which it described as "one of the two most important methods of browser distribution." *United States v. Microsoft Corp., supra*, 253 F.3d at 73.[15] Strikingly, none of the seven computers purchased from each "major OEM" and meticulously examined by Microsoft's experts Drs. Evans and Nichols contained a browser other than IE.[16] The absence of a browser other than IE in the OEM distribution channel is particularly noteworthy in light of the market test provided by the Firefox browser. Despite glowing critical reviews of its innovative features and consumer acceptance demonstrated by a 15% market share, no major OEM has preinstalled Firefox on its new PC systems. Alepin Rep., at ¶ 41 and Kwoka Rep., at ¶ 26.[17]

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[15] The Court of Appeals' description of the significance of the OEM channel of distribution for browsers is consistent with that of the trial court, which characterized it as "crucial." *United States v. Microsoft*, 84 F.Supp.2d 9, 62, 68 (D.D.C. 1999).

[16] The availability of non-Microsoft browsers in the OEM channel has diminished since the trial. In Finding of Fact 239, the Court observed that Navigator was still then available in only 4 of the 60 sub-channels offered by the 15 major OEMs. *United States v. Microsoft, supra*, 84 F.Supp.2d at 69.

[17] Even Microsoft's expert acknowledges that Firefox's claims that it "'has re-ignited innovation and

There is no guarantee that the Final Judgment, if extended, will prove more successful in the future in "prying open" the OEM channel to third-party browsers. Indeed, as the Court knows, the California Group had proposed stronger remedial relief intended to enhance browser competition. Nevertheless, it is too early to conclude definitively that extension of the Final Judgment has no prospect of succeeding in this regard, especially given recent developments like Apple's introduction of its first cross-platform Safari browser. Alepin Rep., at ¶¶ 37-38. Moreover, absent any evidence that the important OEM channel has been pried open to third party browsers, there is no basis for concluding that one of the most important remedial objectives identified by the Court of Appeals has been achieved.

C. Extension of the Final Judgment is necessary to prevent Microsoft from using its entrenched monopoly power to hamper nascent platform threats that are just beginning to emerge

The genesis of the Final Judgment's five-year term was the consent decree negotiated between Microsoft and the settling plaintiffs. This represents a deviation from the normal ten-year term of a DOJ antitrust consent decree.[18] As the United States informed the District Court of Delaware last year in the *Dentsply* case:

> The ten-year term is the standard length sought by the United States in its antitrust judgments. In cases involving dynamic, volatile industries, the United States on occasion has agreed to a shorter length, such as five years. Those are the exceptions, however, because the vast majority of final judgments – even decrees involving relatively dynamic markets – have had terms of 10 years.[19]

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competition on the web'…are not without merit." Iansiti Rep., at ¶ 13.

[18] The five-year reduction in the usual decree term was part of the bargain struck by Microsoft and the settling plaintiffs, an important feature of which was Microsoft's undertaking - still unfulfilled - to make available complete and accurate TD as required by §III.E. Moreover, California Group's Final Judgment is a litigated one and the Court's consideration of the motion to extend it need not be tempered by any consideration of the bargain struck by the parties because there was none.

[19] United States Brief in Support of its Renewed Motion to Enter Final Judgment at 6-7, *United States v. Dentsply Int'l* (March 21, 2006) (No. 99-005 (SLR)), *available at* http://www.usdoj.gov/atr/cases/f215200/215203.pdf.

During the remedies phase of the case, the parties offered what the Court characterized as "limited evidence" on the subject of the proper decree term. *New York v. Microsoft Corp., supra,* 224 F. Supp. 2d at 239-240. On the one hand, Dr. Shapiro testified on behalf of plaintiffs that Microsoft's monopoly power, protected by network effects, was durable and that five years was an insufficient time for competition to develop in such a market. *Id.* On the other hand, Dr. Murphy and Mr. Gates predicted that the pace of development in the industry would be rapid. *Id.*, at 240. Consequently, the Court concluded that the evidence on this issue was "in equipoise" and did not justify imposition of a term longer than the five-year term that Microsoft had negotiated with the settling plaintiffs. *Id.*

Understandably, the Court felt that it was beyond its capacity, or that of any counsel or witness, to predict with certainty the course of events in the industry over the next ten years and the need for a remedy in 2012. *Id.*, at 183-184. Now, however, the Court has the considerable benefit of being able to assess what has transpired in the marketplace since 2002.[20] The central characteristic of the two critical markets in this litigation – PC operating systems and web browsers – has not been rapid product innovation by Microsoft in the intervening five years, but the opposite. Protected by the strong network effects initially described by Dr. Shapiro and explained again by Dr. Kwoka, Microsoft's dominance of both markets has endured - exemplified by market shares greater than 90% for PC operating systems and 80% for browsers. Kwoka Rep., App. 2, Exhs. 1-3. Indeed, absent the spur of competition, Microsoft has introduced just one new version of its dominant PC operating system and web browser since entry of the

[20] The Court can also now evaluate the impact of the severe downturn in IT spending and related post-9/11 recession that occurred during implementation of the Final Judgment. Alepin Rep., at ¶¶ 68, 70 & 71; Kwoka Rep., at ¶ 41.

Final Judgment - both within the past year - Vista in November 2006 and IE 7 in October, 2006. Alepin Rep., at ¶ 24, App. 3; see also Kwoka Rep., at ¶ 46.

The pace of development predicted by Dr. Murphy and Mr. Gates has come largely in other areas of the software industry – not in PC operating systems or web browsers. Microsoft's experts point to developments in web-centric technology like browser plug-ins and add-ons and in applications like calendaring, mapping, photo sharing, online searching and social networking. *See, e.g.*, Iansiti Rep., at ¶¶ 8, 25 & 47 and Evans/Nichols Rep., at §§ 6-8. But neither Microsoft nor its experts assert - as they cannot - that these products and services have yet had any significant impact on Microsoft's dominance of the PC operating system and web browsing markets. Instead, Microsoft's actions in pre-announcing then delaying for several years the release of its new operating system, Vista, effectively froze the pace of adoption of new and alternative technology. Alepin Rep., at ¶¶ 27 & 77.

Because web-centric technologies are so dependent on web browsers and servers for access to consumers, they are particularly susceptible to impediments that Microsoft could interpose were the Final Judgment to expire now. Many of the "new" or "emerging" technologies cited by Microsoft's experts are dependent on a "standards-based" browser to access computing functionality delivered by servers. Alepin Rep., at ¶ 44. For the vast majority of PCs, that browser is IE.

These "emerging" technologies may ultimately pose a threat to Microsoft's Windows monopoly, but only if they remain cross-platform. To remain cross-platform, these technologies require a "standards-based" browser. In other words, the threat that these technologies pose to Microsoft's Windows monopoly through their ability to erode

the applications barrier to entry depends, in large part, on Microsoft's willingness to maintain IE as a standards-compliant browser and to continue supporting cross-platform implementations. See Alepin Rep., at ¶¶ 44 & 77.

But Microsoft has in the past discontinued cross-platform support. *Id.*, at 14. For example, when Microsoft originally distributed IE and competed with Netscape, it distributed versions of IE on several alternative operating systems, including Macintosh, Unix and Solaris. *Id.*, App. 3. Since the Final Judgment was entered, Microsoft has ended support for all IE cross-platform implementations. *Id.* With Vista, Microsoft ended distribution of Flash software – a cross-platform middleware technology identified by Microsoft's experts – and has since announced Silverlight as a direct competitor to Flash. *Id.*, at ¶¶ 56, 57 & 77.

A specific example of how vulnerable these "new" or "emerging" technologies are to manipulation by Microsoft, absent the continued protections of the Final Judgment, is offline internet-centric middleware such as Google Gears and the Adobe Integrated Runtime (AIR, formerly known as Apollo).[21] Each of these recently introduced technologies enables consumers to use Internet-centric applications while offline (i.e, while not actually connected to the Internet) – thereby lessening their reliance on traditional applications. They represent a potential threat to Windows insofar as they are accessible by standards-based browsers from multiple operating system platforms, not just Windows. *See* Alepin Rep., at ¶¶ 56-59 . But should the Final Judgment expire now, Microsoft has the power to tilt the playing field towards its own technology, Silverlight. Microsoft has announced that its next client operating system, Windows 7,

[21] These technologies and Microsoft's competing Silverlight product are described at ¶ 73 of the Iansiti report and at ¶¶ 56 and 57 of the Alepin Affidavit.

will arrive in approximately 2010. Were Microsoft to favor Silverlight in Windows 7 like it did its desktop search technology in the initial Vista release - and as it could absent the protections of the Final Judgment - the platform threat of competing products like Gears and AIR could be severely compromised. *Id.*; *see also* Kwoka Rep., at ¶ 49.

This is not mere speculation. Microsoft has in the past engaged in anti-competitive acts that were neither pro-competitive nor beneficial to consumers in order to protect its monopoly product. The Court has an opportunity now to exercise its broad discretion to extend the Final Judgment to protect emerging technologies that may "pose a threat to its monopoly." *Massachusetts v. Microsoft, supra,* 373 F.3d at 1233. Extending the Final Judgment will not inhibit Microsoft from innovating.[22] It may, however, encourage others to innovate, to introduce new products into markets still largely devoid of competition, and to provide meaningful choice to consumers.

By the time the judicial system was able to address Microsoft's anti-competitive conduct against Netscape and Java in the mid-90's, it was too late for those nascent technologies. Now, there is another opportunity for the Court to protect comparable nascent threats. We urge the Court to do so.

CONCLUSION

For the foregoing reasons, the undersigned plaintiffs respectfully request the Court to extend the provisions of the Final Judgment, except §III.B, until November 12,

[22] *See Judgment of the Court of First Instance, supra* at ¶¶ 53 & 687: "[A]t the administrative hearing, Microsoft stated, in response to a question from the Commission's services, that it had not noticed that the United States settlement had had any negative impact on its incentives to innovate."

2012, and for such other relief as it deems necessary and appropriate.

Dated: October 16, 2007

Respectfully submitted,

FOR THE STATES OF CALIFORNIA. CONNECTICUT, IOWA, KANSAS, MASSACHUSETTS, MINNESOTA AND THE DISTRICT OF COLUMBIA

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