Micro + Soft – The Split Of An Empire Essay, Research Paper

Micro + Soft – The Split of an Empire

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Micro + Soft – The Split of an Empire

Could the megalosaurus business that was conceived in 1975 really be split in two – or three? This is what U.S. District Court Judge Thomas Penfield Jackson has decreed in order to put a stop to the monopolistic shenanigans that Microsoft calls business as usual. The Department of Justice (DOJ) and 20 states are suing Microsoft Corporation in one of the largest antitrust lawsuits brought about since the investigation and ensuing breakup of AT&T in 1984. If Judge Jackson gets his way, Microsoft (MS) could very well be two different companies sparring with each other.

I. Introduction: The Allegations and the Laws

Essentially, the plaintiffs are charging Microsoft with the following three violations:

1) Microsoft has waged an criminal campaign in defense of its monopoly position in the market for operating systems designed to run on Intel-compatible personal computers (PCs). More specifically, the plaintiffs contend that Microsoft violated Section 2 of the Sherman Act by engaging in a series of exclusionary, anticompetitive, and pillaging acts to maintain its monopoly power. They also assert that Microsoft attempted, although unsuccessfully to date, to monopolize the Web browser market, which is also in violation of Section 2 of the Sherman Act. Finally, they claim that some specific measures taken by Microsoft as part of its campaign to protect its monopoly power, specifically, tying its browser to its operating system and entering into exclusive dealing arrangements, are also a violation of the Sherman Act, Section 1 .

II. Introduction: The Proof

The plaintiffs have already shown at trial that MS possesses an extremely dominant, persistent, and increasing share of the relevant market. Microsoft’s share of the worldwide market for Intel-compatible PC operating systems currently exceeds 95 percent, and the company’s share would rest well above 80 percent even if the Mac OS were included in the figures.

The plaintiffs also proved that the applications barrier to entry protects Microsoft’s dominant market share. This barrier ensures that no Intel-compatible PC operating system other than Windows can attract significant consumer demand, and the barrier would operate to the same effect even if Microsoft held its prices substantially above the competitive level for a protracted period of time. Together, the proof of dominant market share and the existence of a substantial barrier to effective entry create the presumption that Microsoft enjoys monopoly power.

Microsoft did not create the barrier to entry all by itself, the consumers’ preferences helped this along, however, Microsoft took specific predatory measures to make sure that its product attracted the market and ultimately trapped the market.

Section 2 of the Sherman Act prohibits the act of monopolization. This means that the act itself is unlawful, not monopolies. It states that “Every person who shall monopolize, or attempt to monopolize, or combine or conspire with any other person or person, to monopolize any part of the trade or commerce among the several States, or with foreign nations, shall be deemed guilty of a felony.” Here is the law – the plaintiffs found the proof. They found it in many of MS’s actions and in their contracts with distributors and they have written testimony, records, and even admissions by MS of their many actions. Yet, MS still maintains that it is not a monopoly.

Unfortunately for MS, there are only two defenses to the allegation of monopolizing that have been acknowledged. One is the defense of innocent acquisition, meaning that they somehow gained acquisition (or purchased) because of superior skills or foresight and that it wasn’t calculated or targeted. The second defense for monopolizing that is recognized is a natural monopoly. This means that there would be a very modest market that could only support one competitor, such as a small town coffee shop, newspaper, or video store. Obviously, Microsoft doesn’t fit into either category, and if it did fit into one of the categories and still abused its power in any plundering or restrictive way, it would lose the defense.

III. Trial

In order to fully present the history and the situation as it stands, I have included a table that shows a subset of the major events leading up to the present status of the case against Microsoft. It demonstrates just how long this type of case can persevere and how much time, money, and effort are involved. (See Table 1).

Table 1

Trial Timeline

Date of Event: Important Details:

Oct. 20, 1997

The Justice Department sues Microsoft, asserting that the company violated a 1995 court order and consent decree resolving an earlier government lawsuit against Microsoft. The government asks for a record $1 million per day in fines.

Dec. 11, 1997

U.S. District Judge Thomas Penfield Jackson orders Microsoft to stop requiring computer makers to distribute Internet Explorer with its 95 operating software. The ruling also applies to the upcoming Windows 98 program, in which IE is even more integrated with the operating software.

Dec. 15, 1997

Microsoft files an appeal with the U.S. Court of Appeals. The company argues that it was an error for the court to forbid Microsoft from bundling IE 4.0 with Win95 after denying the Justice Department’s claim that Microsoft violated the 1995 consent decree. Microsoft says it will comply with the injunction while it is on appeal.

Jan. 8, 1998

Microsoft executives express regret for the company’s harsh rhetoric against the Justice Department and say the software giant should have been more respectful of the court and prosecutors. (In an ABCNEWS.com poll on Jan. 9, 72% of the 2,500 respondents believed that Microsoft had been disrespectful to the Justice Department and the court.)

Jan. 22, 1998

Microsoft and the Justice Department settle their dispute. Microsoft agrees to offer an IE-free Windows.

May 5, 1998

Microsoft asks a federal appeals court to rule that Judge Jackson’s Dec. 11 preliminary injunction imposing restrictions on Windows 95 “or any successor” do not apply to Windows 98.

May 18, 1998

The Justice Department and 20 state attorneys general sue Microsoft for antitrust violations, including tying the browser to the operating system and using anti-competitive contracts with computer makers and Internet service providers (ISPs).

June 23, 1998

The U.S. Court of Appeals reverses the lower court’s decision in the Windows 95 consent decree case, allowing Microsoft to ship Windows 95 with browsers.

Aug. 31, 1998

In response to a routine filing by Microsoft, the DOJ makes its first references to Microsoft’s business dealings with other companies, including Apple, Intel, Sun Microsystems and Caldera.

Oct. 19, 1998

After a number of delays, the case of U.S. vs. Microsoft begins in U.S. District Court in Washington, D.C. Then-Netscape CEO Jim Barksdale is the government’s first witness.

Nov. 17, 1998

In a separate court case, Sun Microsystems wins a preliminary injunction against Microsoft, forcing Microsoft to stop producing and distributing Java technologies that don’t comply with Sun’s standards. Decisions in this and other antitrust cases involving Microsoft could affect the federal case.

June 1, 1999

With no word of any possible settlement forthcoming, both sides are expected back in court on this date to present rebuttal witnesses and closing arguments.

June 2, 1999

Microsoft began defending itself in a federal court in Connecticut against Bristol Technologies, which claims antitrust violations after Microsoft refused to license Windows source code to Bristol. An antitrust suit by Caldera, filed in 1996, also began this month.

Sept. 22, 1999

One day of closing arguments.

Nov. 5, 1999

Judge Jackson rules that the software company does indeed hold a monopoly thanks to its pervasive Windows operating systems, that it abused its monopoly power and that this abuse has harmed potential competitors and consumers. The judge’s finding of fact is the first of three rulings that will determine Microsoft’s fate.

April 3, 2000

Judge Thomas Penfield Jackson rules that Microsoft violated the Sherman Antitrust Act, and is also liable in 19 state suits. Microsoft said it will appeal.

May 24, 2000

Judge Jackson confirms MS’s violations of the Sherman Antitrust Act, and rules to split up the company.

June 20, 2000

Judge Jackson granted a request to stay the conduct remedies until a higher court acts and sent the case to the Supreme Court for consideration.

IV. The Proposal

The Government proposed the following to control Microsoft and bring them down a notch or two:

Microsoft shall be split into two companies, one for its Windows operating system and one for software applications, such as Microsoft Office and Internet Explorer. The government is requesting that Microsoft would have to submit a breakup plan four months after the final ruling of U.S. District Court Judge Jackson. The two separate companies brought into existence would be prohibited from merging or forming any joint ventures with each other. Separate boards of directors for the two companies would be established and kept apart. The government requested that the terms of the breakup plan would last ten years. Other controlling, yet temporary restrictions would also be imposed on Microsoft until the appeals process was completed.

In addition to breaking Microsoft in two, the Justice Department would demand the following restrictions: 1) Temporary uniform standards would have to be adopted for licensing the Windows operating system to other makers of personal computers. 2) Personal computer makers would be allowed to modify the appearance of the Windows operating system. 3) No actions of retaliation could be taken by the two companies against those who gave evidence to the federal government against Microsoft or submitted testimony. 4) A temporary ban would be placed on Microsoft to prevent any threats or acts against personal computer makers.

Here is an illustration of what the make up of a Microsoft Applications Company might look like: Microsoft Office, BackOffice, Internet Explorer, Mobile Explorer, Outlook Express, Frontpage Express, Net Meeting, and other browsers, e-mail clients and related tools. Slate online magazine, Expedia travel network, the Microsoft network, MSNBC. Streaming audio and video client and service software, media player, voice recognition software, Java virtual machine software. Developer tools, consumer hardware, transaction server software, XML servers and parsers, Microsoft Management Server SNA server software, indexing server software, Internet Information Server. This would also extend to investments owned by Microsoft in connection with partners, joint venturers, original equipment makers, independent hardware vendors, independent software vendors, distributors, developers, and promoters of Microsoft products or in other information technology businesses.

And, the other new company – here is what the make up of a Microsoft Operating Systems Company might look like: Windows 95, Windows 98, Windows 2000 Professional, and their successors, including Windows operating systems for personal computers code-named “Millennium,” “Whistler,” “Blackcomb,” and their successors. Development, licensing, promotion and support for computing devices, including personal computers, other computers based on the Intel x-86 or competitive microprocessors such as servers, handheld devices and television set-top boxes.

This would of course also include the personnel, facilities and other assets associated with those businesses. It would be able to hold a license to continue distribution of the existing Internet Explorer code, but it will have to develop its own browser in the future under new strategies.

V. Microsoft’s Response

Obviously, Microsoft was less than happy with the proposal put forth by the government and did not intend to back down. They saw the DOJ’s proposal as too harsh and overly extreme under the circumstances. Microsoft spokesman, Jim Cullinan likened the proposal of giving up their intellectual property to competitors like Sun and Oracle, to “?forcing Coke to share its secret formula with Pepsi and every other major soft drink vendor in the country.” And CEO Steve Ballmer called the government’s plan to split the company like “?splitting up a rock band because of its popularity.”

At the Judge’s request, Microsoft tendered their own proposal to the courts on May 10, asking that the Judge punish them in the area of their business conduct, but not break the company in two. Critics viewed Microsoft’s counter proposal of their own judgment as not much more than a slap on the wrist and do not expect that the courts will accept it. Ironically, if Microsoft had intended to actually do some of the “nice play” techniques that they are now proposing, maybe they wouldn’t be on trial. So far, the government’s opinion is that Microsoft has merely come up with a transparent cosmetic remedy that will not have much impact on the competitive issues. “What remedy does Microsoft propose to undo the damage to competition caused by its past illegal conduct?” the government wrote, “Nothing.”

Alternatively, Microsoft’s counter proposal was viewed by many as being very soft. Listed here below are the fundamental pieces:

1) They [Microsoft] will ensure that Microsoft will not cancel or refuse to grant a Windows license agreement to a PC maker because the PC maker ships or promotes other non-Microsoft software.

2) They will allow PC makers to include as many icons for non-Microsoft software as they choose on the Windows desktop.

3) They will allow computer users to choose which Web browser they want to use during Windows’ initial boot sequence.

4) They will allow PC makers to remove the Internet Explorer web browser icon from the Windows desktop and start menu.

5) They will refrain from promoting another company’s product on the Windows desktop in exchange for that company’s agreement to limit its distribution of non-Microsoft software.

6) They will ensure that independent software vendors have timely access to technical information called “application programming interfaces” needed to write Windows applications.

7) They will continue to license a predecessor operating system after the release of a new version of Windows so that computer makers could use the old one if they didn’t like the features in the old one.

8) Microsoft has proposed that all of the above restrictions remain in place for four years instead of the ten as requested by the government, stating that nothing in the record would justify such a long term for relief.

In their filings made with the U.S. District Court with their own proposals, Microsoft asserted that Judge Jackson’s previous findings did not warrant the extreme measure of dividing the company in two. “In stark contrast to the relief sought in its complaint, the government seeks to rip apart the company that until recently had the largest market capitalization in the world – an extreme remedy not even hinted at in the government’s complaint,” stated one of Microsoft’s last filings. Microsoft claimed that the DOJ’s proposed solutions are too harsh and still maintains that they should be trusted and will make good on their proposed remedies. Unfortunately, had they gone this direction in the first place when the original complaints started cropping up, maybe they could be trusted to keep their word.

VI. The Foes and Their Thoughts

Microsoft’s determination and perseverance in the quest for new markets is anything but good news for competitors. The company is definitely a force to be reckoned with wherever it attacks because of its billions in cash stock-pile and the power of its Windows monopoly. Certainly their rivals would like to see the wind let out of their sails a bit. Some of the competitors that would like to see the split up of Microsoft are: Sun Microsystems, Oracle, Red Hat Software and Corel (both deal in Linux), Dell Computer, and Apple Computer.

Although the rivals seem to happy with the direction that the case has taken and the recent rulings, they are still skeptical because Microsoft is just as powerful today as it was when this case started. This, according to Michael Morris, chief general counsel for Sun Microsystems, one of Microsoft’s most hostile adversaries. Morris went on to suggest that the courts now figure out how to bring about “significant remedies to break Microsoft’s hold on the browser market.” Sun has always felt that Microsoft’s methods were bullying and that they have continuously abused their wealth of power to gain control in the marketplace.

Another embittered rival, Jim Barksdale, former chief executive of Netscape, indicated that the ruling was very satisfying to a lot of people that worked so hard at Netscape over the years. He indicated that the judge was finally agreeing with what they [Netscape] have been saying for approximately four and a half years; that Microsoft will stop at nothing. This seemed to be the general opinion among the competitors; that Microsoft pretends to act friendly and play by the rules, but that they are essentially only out for their own good and will indeed stop at nothing until they are the most powerful and can move the market around like their own personal pawn in a chess game.

VII. Current Status and Discussion

I have included some excerpts from the court’s April 2000 findings in the ruling against Microsoft. The conclusions show undoubtedly, that Microsoft acted with deliberate intent to harm its competitors.

Viewing Microsoft’s conduct as a whole also reinforces the conviction that it was predacious. Microsoft paid vast sums of money, and renounced many millions more in lost revenue every year, in order to induce firms to take actions that would help enhance Internet Explorer’s share of browser usage at Navigator’s expense. These outlays cannot be explained as subventions to maximize return from Internet Explorer. Microsoft has no intention of ever charging for licenses to use or distribute its browser. Moreover, neither the desire to bolster demand for Windows nor the prospect of ancillary revenues from Internet Explorer can explain the lengths to which Microsoft has gone. In fact, Microsoft has expended wealth and foresworn opportunities to realize more in a manner and to an extent that can only represent a rational investment if its purpose was to perpetuate the applications barrier to entry. Because Microsoft’s business practices “would not be considered profit maximizing except for the expectation that … the entry of potential rivals” into the market for Intel-compatible PC operating systems will be “blocked or delayed,” Microsoft’s campaign must be termed predatory. Since the Court has already found that Microsoft possesses monopoly power, the predatory nature of the firm’s conduct compels the Court to hold Microsoft liable under ? 2 of the Sherman Act.

In this case, Microsoft early on recognized middleware as the Trojan horse that, once having, in effect, infiltrated the applications barrier, could enable rival operating systems to enter the market for Intel-compatible PC operating systems unimpeded. Simply put, middleware threatened to demolish Microsoft’s coveted monopoly power. Alerted to the threat, Microsoft strove over a period of approximately four years to prevent middleware technologies from fostering the development of enough full-featured, cross-platform applications to erode the applications barrier. In pursuit of this goal, Microsoft sought to convince developers to concentrate on Windows-specific APIs and ignore interfaces exposed by the two incarnations of middleware that posed the greatest threat, namely Netscape’s Navigator Web browser and Sun’s implementation of the Java technology. Microsoft’s campaign succeeded in preventing – for several years, and perhaps permanently – Navigator and Java from fulfilling their potential to open the market for Intel-compatible PC operating systems to competition on the merits. Because Microsoft achieved this result through exclusionary acts that lacked procompetitive justification, the Court deems Microsoft’s conduct the maintenance of monopoly power by anticompetitive means.

Microsoft has shown the courts and indeed the world, time and time again that they (think) are impervious to the laws that govern other firms. They continue to have their hand slapped and then it’s back to the old standard of whip out the checkbook, pay the fine, and on to the next business to be crushed, or the next laws to be violated. Microsoft thinks they are so powerful already that they are above the law. The government is now more than ever convinced that the only way to get Microsoft’s attention and possibly putting an end to their unlawful practices, is to play rough with them. This means sticking by their proposal and convincing the judge to impose it. In the 70 page brief filed, the DOJ stated that they believe that breaking up the company is the only way to prevent Microsoft from continuing with their anticompetitive behavior.

It is likely that the all-conclusive final ruling will end up somewhere in between the government’s extreme proposal of splitting the company and MS’s proposed spanking, but followers of the case and analysts alike believe that the final remedy judgment will lean more toward the government’s side than Microsoft’s. Of course, Microsoft will surely appeal again and again.

It is not likely that Microsoft will get off so easily this time and it is their just due since they cannot be trusted to keep their word. Once again, using their strength and power to bully their way into other market segments, with their introduction of Windows 2000?, Microsoft has included other software that will only run if the user purchases one version of Windows 2000 for their desktop and yet another for their server that runs their network. Microsoft will deny that they are abusing their position of course, as they have in the past, but Federal and State “trustbusters” believe differently.

In the midst of all the chaos of trial and government rulings, Microsoft has still pushed forward with yet another package into yet another market they wish to conquer and dominate. They have continuously maintained that they are not bullying their way into other markets by means of their monopolistic strength, but merely providing the world with better tools with which to do their jobs. What is wrong with this? Depending on how you view their statements, there could be plenty wrong with this type of actions. Microsoft continues to make falsiloquiums. The definition of a falsiloquium is a false statement, when the purpose of the statement is to hide from the receiver what is truly on one’s mind and the receiver can safely assume that this is indeed the purpose of the statement. Microsoft will continue to assert that they are not abusing their position of power, yet still be fully aware that everyone knows that they [Microsoft] know they are.

The case is now currently (slightly) delayed and the conduct remedies previously put in place by Judge Jackson are stayed until heard by a higher court. The conduct changes were originally slated to be put in place on September 5, 2000, so Microsoft has indeed received a bit of reprieve. For now.

Microsoft would have preferred that the case be sent directly to the appellate court, where it has previously enjoyed successes, but it is also not unhappy by the surprising stay of the restrictions. It has given them some room to breathe. Hopefully, they won’t take advantage of it this time.

VIII. Recommendations

The obvious recommendations in this case are all the considerations, fair play, and non-aggressive marketing of their products that Microsoft chose not to employ over the past five years. I have said this repeatedly throughout the paper; if Microsoft had intended to actually do some of the “nice play” techniques that they have now volunteered to do, maybe they wouldn’t be in this mess. All other corporations should take heed; if indeed the courts are making a statement by taking on Microsoft, then it is for a reason. If others want to avoid this type of determined pursuit from the government and their angry competitors, they should obey and pay close attention to the rules of the Sherman Act.

The Sherman Act was put in place in 1890 to prevent people and businesses from becoming monopolistic and practicing unfair trade and methods of competition. The Sherman Act is also the only antitrust act that grants criminal penalties. This means that corporations could be fined up to $10 million per violation and individuals can be fined up to $350,000 per violation plus up to three years in prison. The reason that the penalties are so harsh is because the necessary element for criminal liability under the Sherman Antitrust Act is intent. Microsoft did have intent to practice unfair competition. Microsoft did have intent in all of its unlawful conduct and in its business contract relationships.

The biggest question is not whether or not Microsoft can sustain the split up of the company, but whether the world will then end up with two mini-monopolies. The proposed division will still allow both companies (maybe more) to go forward with their objectives, still make profit, and continue to expand in their markets. The breakup, however, would still leave consumers with an operating-systems monopoly and an applications monopoly that could very well lead to double marginalization, meaning that we might have a substantial software mark-up on both sides.

This will be the challenge that the courts have in enforcing the antitrust law and using this case to control Microsoft. If they can still push forward with the proposed split of the company with all the conduct remedies in place, Microsoft will be forced to comply and modify their methods of doing business. They will not be able to merge or form any joint ventures with each other. Independent boards of directors for the two companies will have to be conceived and kept separate. The original government request was that the terms of the breakup plan be for a term of not less than ten years; if they can enforce it, maybe Microsoft will learn to change its ways.

With the split, the two or more emerging companies will need to follow the outlines of their restrictions very carefully, so as not to violate the court ruling, but also to be able to go forward as separate companies and be able to meet their objectives. They will be watched, not just by the court system, but by the entire world to see if they can pull through this drastic measure that needs to be taken in controlling the unfair competition. Each company will need to avoid all attempts and conspiracies to monopolize, restrain trade, or practice any type of predatory or exclusionary acts in their dealings with competitors and distributors.

The bottom line is that companies such as Microsoft nurture government involvement and regulation enforcement in businesses by their continued aggressive behavior and thus make it worse for other corporations. Microsoft needs more than just their wrist slapped this time, they need to be put on an extremely tight leash and if that means splitting them up and forcing the two to compete against each other, then let the games begin.

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