Uncertainty reigns

Microsoft has decided to throw in the towel and concede defeat in its antitrust battle with the European Commission. Other IP owners would do well to look carefully at what it all means to them

By **Duncan Curley**

"Customers want integration, and they want choice. To some extent, those things are at odds" said Larry Ellison, CEO Oracle Corporation, in an interview with the Financial Times (17th April 2006).

On 22nd October 2007, Microsoft announced that it was throwing in the towel in its long-running battle with the European Commission over the controversial 2004 decision to fine the company Euros 497 million for breaching EU competition law.

Microsoft's admission of defeat came almost a decade after the dispute had kicked off with an exchange of letters in the autumn of 1998 between senior officers at the company and one of its major competitors, Sun Microsystems Inc. This, in turn, led to a complaint to the European Commission and the involvement of the regulator. After a long investigation, the Commission concluded that Microsoft had abused its dominant position on the market for PC operating systems, contrary to European competition rules (Article 82 of the EU Treaty).

The judgment of the Court of First Instance of the European Communities (the CFI) on 17th September 2007 substantially upheld most aspects of the Commission's original decision. It appears to mark the end of Microsoft's attempts to exonerate itself, although questions remain as to whether the company can satisfy the Commission that it is now complying with the detailed terms imposed by the original ruling.

Now that the dust has begun to settle, the question remains as to whether any broader significance should be attached to Microsoft's defeat in the EU. Is there anything of special significance for IP owners to learn from the latest developments? Or can we assume that the CFI's decision is a one-off ruling, directed at a company with a unique market position that imported a special responsibility to Microsoft that is unlikely to be replicated in other areas of business activity?

Protecting competition – or competitors?

Central to the EU case (and the earlier US case) was Microsoft's very strong position on the market for PC operating systems. PC operating systems deal with routine tasks such as memory allocation and controlling the operations of peripherals, such as printers. The Windows operating system has, of course, become the *de facto* standard for most PCs. The fact that Windows is ubiquitous undoubtedly confers upon Microsoft significant market power. However, consumers also benefit because they get access to many kinds of application software that have been written specifically to interface with Windows.

Antitrust laws in both the EU and the US constrain the kinds of business practices that may be undertaken by companies with such a strong market position. In the US *Microsoft* case, the Department of Justice alleged that Microsoft had attempted to maintain a monopoly position in the market for PC operating systems, by (for example) including Internet Explorer with Windows. Part of the US case involved an examination of Microsoft's conduct in relation to a competitor, Netscape, and its internet browser, Navigator. Much of the case was taken up with analysis of colourfully worded internal Microsoft documents concerning the threat posed by Netscape and what

Microsoft's response should be to that threat. Although the Department of Justice scored a notorious victory in the first round (at district court level), after a number of reversals on appeal, the US case settled.

There are conflicting views as to the rationale behind the US settlement. Some think that Microsoft got off lightly, benefiting from a political change in the US administration. Others argue that many of the original allegations against Microsoft were lacking in substance and the case was one that should have been treated with scepticism from the outset; bearing in mind that the source of much of the agitation about Microsoft's alleged anti-competitive activities was Microsoft's competitors.

It is at least noteworthy that the EU case gained traction with the European Commission after a complaint from one of Microsoft's competitors – Sun. Sun asked Microsoft to disclose technical information to allow it to achieve interoperability between its own server products and the Windows environment. A server is essentially a powerful computer that typically includes both hardware devices and software, such as an operating system, mostly for facilitating the management of communication between users. The information requested by Sun was intended to allow it (Sun) to produce work group server operating systems that provide (for example) file and print services to a group of PCs, facilitating common access by a network of PC users to shared services. In short, Sun wanted to be able to compete more effectively with Microsoft on the market for work group server operating systems.

Refusals to deal and tying

EU competition law may forbid a refusal to deal by a dominant company, in certain circumstances. Microsoft's refusal to disclose the information requested by Sun was investigated by the Commission as a potential breach of Article 82, with the Commission formally commencing proceedings against Microsoft in August 2000.

A further line of complaint against Microsoft was pursued later (in August 2001) by the Commission. This concerned the integration (or bundling) by Microsoft of its Windows Media Player into its Windows operating system, categorised in legal terms by the Commission as a "tying" abuse under Article 82. In other words, the allegation was that Microsoft was making the availability of the Windows PC operating system conditional on the simultaneous acquisition of Windows Media Player.

The Commission's decision

After a long investigation, the European Commission decided that it had established a firm factual basis for Microsoft's dominant market position and the activities that had taken place. The parties failed to agree a settlement and this led to the Commission's decision of 29th March 2004 in which Microsoft was fined for breaching Article 82. A number of remedies were also imposed. While Microsoft challenged many of the Commission's findings of fact on appeal, the interesting sections of the CFI's judgment concern the arguments made on appeal in relation to the remedies.

The Commission had ordered Microsoft to disclose the relevant interoperability information, specifically: "complete and accurate specifications for the protocols used by Windows work group servers"; the protocols being the rules of interconnection and interaction between the Windows client PC operating system and the Windows work group server operating system (interoperability information). The Commission stressed in its decision that by asking for "specifications" it was not requiring Microsoft to disclose its own implementations of those specifications, ie source code. The disclosure was to be made on reasonable and non-discriminatory terms. The remedy in the Windows Media Player part of the case was to force Microsoft to offer its Windows operating system without a media player.

Disclosure of interoperability information

Microsoft put forward numerous protests to counter the Commission's position. Microsoft contended that the interoperability information sought would allow Microsoft's competitors simply to clone (or copy) Microsoft's products. Microsoft maintained that the interoperability information constituted valuable trade secrets that Microsoft should be allowed to keep to itself. It said that the information was protected from use by third parties by means of various IP rights held by Microsoft, including copyright and patents.

To allow others to use the interoperability information would be tantamount to forcing Microsoft to grant compulsory licences under its IP. This would have an adverse effect on Microsoft's incentives to innovate. After all, why should Microsoft invest in research and development, and develop new and innovative products, if competition law then forces the technology to be licensed out to others?

The *Magill* and *IMS Health* cases

One area of the law where it was hoped that the CFI would provide some clarity for IP owners was the question of when competition law might compel the disclosure of technical information and the licensing of technology and IP rights to competitors. The *Magill* case from the 1990s was concerned with copyright subsisting in a list of TV programmes. It was at the culmination of that case that the European Court of Justice held that a refusal to license an exclusive IP right (such as copyright) may, in exceptional circumstances, constitute an abuse of Article 82 that warrants the imposition of a compulsory licence. At the time, many commentators dismissed the notion that the *Magill* decision could bring competition law into play whenever large firms were exercising their IP rights; the decision was thought to be unique, no doubt (at least in part) due to the weak nature of the rights in question in that case.

In the subsequent *IMS Health* case, the European Court of Justice said that in order for competition law to have an impact on a refusal to grant a licence, the IP owner's refusal must prevent the emergence of a product for which there was potential consumer demand. The conclusion from both the *Magill* and *IMS Health* cases was that Article 82 rarely mattered to IP owners. It would require the existence of a dominant market position and exceptional circumstances involving consumer demand for a product (and a refusal to license by the dominant company) before Article 82 would come into play.

In an attempt to win hearts and minds, Microsoft made a big play on encroachment upon its IP rights, at one point comparing the forced disclosure of the interoperability information as being akin to "opening the vaults of a bank" and "handing out money to passers-by".

Unbundling Windows Media Player

According to the Commission, Windows Media Player and the Windows operating system are two separate products. Bundling the two products together (without offering them separately) works against the interests of consumers. The Commission said that if the practice were allowed to continue, it would lead to the progressive elimination of rival media players, as producers of compatible software and content knew that if they based their products on Microsoft's Windows Media Player technology – rather than on competing technology – they would be able to reach almost all PC users. This would eventually lead to all consumers preferring Windows Media Player (with a wider range of complementary products) to other media players.

For its part, Microsoft maintained that the Commission had got its facts wrong and said that content providers encoded in a number of media formats, and as such the threat from Windows Media Player was illusory. The company also argued that the Commission was forcing it to offer to consumers what was essentially a degraded version of its Windows operating system, a remedy that was not appropriate to cure the alleged infringement of competition law.

The judgment of the CFI

Microsoft's resounding defeat in the CFI has already been well documented. The CFI is a difficult forum for overturning facts, especially on economic questions, where the CFI will usually defer to the Commission's analysis, unless it has made a serious error. Having rejected all of Microsoft's attacks on the Commission's major findings of fact, the CFI then moved on to consider the Commission's application of EU competition law to those facts.

It is clear from the judgment that the CFI considered the legal arguments of both sides in detail, but in the end it was satisfied that the Commission had correctly applied the principles on all of the major points. Only on one narrow procedural issue did the CFI overturn the Commission (concerning the monitoring trustee appointed to oversee compliance with the Commission's 2004 decision).

Confused signals

There will usually be some alternative products on the market that constitute a competitive challenge to the position of IP owners. This is why Article 82 is rarely an issue for them. However, on the Commission's own findings in the *Microsoft* case, there were already a number of alternative providers of work group server operating systems (with a significant proportion of overall market share between them), including the main rival to the Windows operating system, NetWare (sold by Novell) and Linux and UNIX. Nevertheless, the Commission decided that Microsoft's refusal to disclose interoperability information was such a threat to future competition that a behavioural remedy and a fine under Article 82 were necessary.

The Commission's order effectively means that third parties will be able to access and use certain of Microsoft's software communications protocols and specifications under licence. The Commission hopes that its remedy will see the market open up to more competition, with companies taking advantage of the availability of interoperability information to innovate and produce new work group server operating systems that will be compatible with Windows PC operating systems.

It remains to be seen whether the licensing programme ordered by the Commission will encourage more companies to enter the market and thereby promote competition. One of the terms of settlement of the US case was that Microsoft should make available a licensing programme for client-server protocols, on reasonable and non-discriminatory terms. The take-up has not, apparently, been great (21 licensees, as of January 2005).

As for Microsoft's IP rights that are to be licensed together with the protocols and specifications, the Commission maintained that any possible adverse effect on Microsoft's incentives to innovate will be offset by the positive effect on the level of innovation and competition that will result in the rest of the industry, by allowing other companies to access the server operating systems market effectively. The exceptional circumstances in this case that warrant a compulsory licence were said (by the Commission) to be Microsoft's large share of the PC operating systems market and the fact that Microsoft had changed its business practices over time in relation to the supply of interoperability information; from making such information available (when Microsoft

first entered the market) to refusal, by the time of Sun's request in 1998.

Crystal ball?

It will be appreciated that much of the Commission's reasoning was based on speculation as to future behaviours, albeit grounded in economic theory. This leads one to pose the question as to whether the commercial scale of Microsoft's alleged infractions of competition law posed such a concrete and serious threat to consumers as to warrant the significant investment that has been made (in terms of the Commission's resources, not to mention the size of the fine imposed), bearing in mind also the fact that the dispute started life not as a result of any consumer complaints, but as a part of an ongoing global dispute between two large multinational corporations (Sun and Microsoft).

For those who believe that most markets will sort themselves out if left alone, the attempt by the Commission to fix something that may not even have been broken was one of the unsatisfactory aspects of the initial decision. Nevertheless, from a strict legal standpoint, the CFI was satisfied with the Commission's assessment under the criteria laid down in Article 82.

More uncertainty

Somewhat disappointingly for IP owners, the CFI did not elaborate further on the "exceptional circumstances" test referred to in *Magill* and *IMS Health*. If anything, the CFI's decision in *Microsoft* has left the law in an even more uncertain state. As a result, IP owners with a strong market position would be well advised to consider carefully any refusals to deal with a putative licensee. We may see an increase in complaints to competition regulators (and possibly the courts) from disgruntled companies that have been refused a licence, citing the *Microsoft* case and bringing themselves under what now appears to be a broad umbrella of "exceptional circumstances".

Although the Commission's battle with Microsoft has taken up many thousands of pages in the business and the specialist legal press, the facts of the case seem to indicate a relatively narrow compass of dispute in two highly specific areas of technology. After the CFI's decision, a representative of ECIS, a trade association representing rivals of Microsoft such as Adobe and IBM, acclaimed Microsoft's acknowledgment of defeat as a significant step forwards. The open source community has certainly welcomed the decision and certain companies (eg, Samba) may decide to use the interoperability information made available by Microsoft in the development of work group server operating systems that can be used by businesses as an alternative to Microsoft products.

Since the Commission's decision, Microsoft has settled with most of the parties that were originally involved in the case (including Sun). It has made available to prospective purchasers Windows XP Home Edition N and Windows XP Professional Edition N – versions of Windows without Windows Media Player. Consumers so far have shown no desire for these products and they have not been a commercial success.

As far as interoperability information is concerned, Microsoft has put in place a European server protocol licensing programme and IP licence agreements have been made available on Microsoft's website to allow third parties to develop and distribute Windows-compatible server operating systems. Although the Commission said last year that it was not satisfied that Microsoft had complied with its disclosure obligations (and fined the company a further Euros 280.5 million), Microsoft has said in a recent press release that it intends to comply with the Commission's ruling. It seems that this marathon case is moving into its final phase. Only time will tell as to whether the European Commission's victory over Microsoft will secure more innovation and competition from new products, with tangible benefits for European businesses and consumers. ■

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