

MICROSOFT CHAMPIONS INTELLECTUAL PROPERTY
RIGHTS AND LOSES TO EUROPEAN UNION COMPETITION
LAW: *PROCEEDING UNDER ARTICLE 82 OF THE EC
TREATY CASE COMP/C-3/37.792 MICROSOFT, MARCH 24, 2004*

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I. INTRODUCTION

In March 2004, the Commission of the European Communities (“the Commission”) reached a decision against Microsoft Corporation (“Microsoft”) for its anticompetitive practices, concluding five years of investigation and preliminary proceedings.¹ First, the Commission imposed a fine on Microsoft for a record amount of €497,196,304 (about \$635 million). Second, it required Microsoft to provide interoperability information for any company interested in developing and distributing workgroup server operating system products. Last, it required Microsoft to offer a fully-functioning version of its Windows PC Operating System able to be configured so it no longer includes Windows Media Player. This decision paralleled the recent decisions in the United States on antitrust issues with “middleware” and Microsoft Internet Explorer. However, the two governments’ courts reached different conclusions, much to Microsoft’s favor in the United States and disfavor in the European Union.

Microsoft views these cases as a battleground for the intellectual property rights that all technical companies value and believes that these rights should be given the highest priority in order for high-technology companies to survive. Unfortunately for Microsoft, the courts on both sides of the Atlantic find antitrust laws to serve a higher public good than that served by the supremacy of intellectual property rights.

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1. See COMMISSION DECISION OF 24.03.2004 RELATING TO A PROCEEDING UNDER ARTICLE 82 OF THE EC TREATY (CASE COMP/C-3/37.792 MICROSOFT), ¶¶ 3–13 (Apr. 21, 2004), available at <http://europa.eu.int/comm/competition/antitrust/cases/decisions/37792/en.pdf> [hereinafter COMMISSION DECISION].

II. FACTUAL AND PROCEDURAL BACKGROUND

A. *The European Commission's Decision*

At the end of 1998, Sun Microsystems, Inc. ("Sun") applied for the initiation of proceedings against Microsoft at the Commission.² The original complaint addressed only the issue of interoperability, but was subsequently expanded by the Commission to include the incorporation of another product with the Microsoft Windows operating system ("Windows"), namely, Windows Media Player ("WMP").³ During the investigation, the Commission collected market information from forty-six customers provided by Microsoft and over 133 responses from companies active in areas involving each of the two issues.⁴ An oral hearing took place in November 2003 and Microsoft, Sun, and other interested third parties were allowed to file materials on the two issues until February 7, 2004.⁵

B. *United States Federal Proceedings*

In 1998 and 1999, the U.S. government, nineteen individual states, and the District of Columbia filed an action against Microsoft that resulted in a lengthy trial.⁶ The United States alleged four violations of the Sherman Act:⁷ (1) violation of § 1 for entering into exclusive dealing arrangements; (2) violation of § 1 for tying Microsoft Internet Explorer to Windows; (3) violation of § 2 for the maintenance of a monopoly in the personal computer operating system market; and (4) violation of § 2 for attempted monopolization of the Web browser market.⁸ The Court issued its findings of fact in 1999⁹ and, after unsuccessful settlement negotiations,¹⁰ issued its conclusions of law in 2000.¹¹ The district court found in favor of the plaintiffs on the tying violation of § 1,¹² the monopolization violation of § 2,¹³ and the attempted monopolization

2. *Id.* ¶ 3.

3. *Id.* ¶¶ 3–5.

4. *Id.* ¶¶ 6–9 (including over one hundred responses on interoperability and thirty-three responses on WMP).

5. *See id.* ¶¶ 11–13 (listing the interested third parties as the Association for Competitive Technology; Time Warner, Inc.; Computer & Communications Industry Association; Computing Technology Industry Association; Free Software Foundation Europe; Lotus Corp.; Novell, Inc.; RealNetworks, Inc.; and Software & Information Industry Association).

6. *United States v. Microsoft Corp.*, 87 F. Supp. 2d 30, 35 (D.D.C. 2000).

7. Sherman Antitrust Act, 15 U.S.C. §§ 1–7 (2000).

8. *Microsoft Corp.*, 87 F. Supp. 2d at 35.

9. *United States v. Microsoft Corp.*, 84 F. Supp. 2d 9 (D.D.C. 1999).

10. Kathleen A. Marron & Heidi E. Viesturs, *Competition Beyond the Year 2000: An Overview of Antitrust, Predatory Pricing, Competitive Access, Overbuilds, and Other Competitive Issues in Telecommunications*, 622 PLI/Pat 667, 698–700 (2000).

11. *Microsoft Corp.*, 87 F. Supp. 2d at 30.

12. *Id.* at 47–51.

13. *Id.* at 37–44.

violation of § 2.¹⁴ However, it ruled against the plaintiffs on the exclusive dealings violation of § 1.¹⁵

On review, the U.S. Circuit Court of Appeals for the District of Columbia reversed the finding of attempted monopolization of the Web browser market, remanded the tying issue to the trial court, and upheld in part and reversed in part the finding that Microsoft maintained a monopoly in the operating system market.¹⁶ The remedy imposed by the lower court was also remanded.¹⁷ After the Circuit Court's decision, half of the states involved in the lawsuit (the "New York group")¹⁸ and the U.S. government reached a settlement, while the other half of the states involved in the lawsuit (the "California group") went to trial.¹⁹ The judge ultimately found the settlement involving the New York group to be appropriate and incorporated it into the ruling on the California group's complaint.²⁰ One state, Massachusetts, chose to appeal, and the Circuit Court unanimously affirmed the lower court's decision.²¹

III. THE EUROPEAN COMMISSION'S FINDINGS

A. Interoperability

"Interoperability"—defined by the Commission as "the ability to exchange information and mutually to use the information which has been exchanged"—was derived from an earlier European Council Directive.²² The Commission defined the relevant market and analyzed Microsoft's position in that market, then concluded that Microsoft held a dominant position or quasi monopoly.²³ This dominant position had effectively required competitors' products to be compatible with Windows products in order to compete in the market.²⁴

In order to find that Microsoft had violated European competition law, the Commission would have to conclude that Microsoft abused its dominant position.²⁵ The legal standard to determine the abuse is an

14. *Id.* at 45–46.

15. *Id.* at 51–54.

16. *United States v. Microsoft Corp.*, 253 F.3d 34, 46 (D.C. Cir. 2001) (per curiam).

17. *Id.*

18. *See United States v. Microsoft Corp.*, 231 F. Supp. 2d 144, 150 n.1 (D.D.C. 2002). This group is composed of Illinois, Kentucky, Louisiana, Maryland, Michigan, New York, North Carolina, Ohio, and Wisconsin. *Id.*

19. *See New York v. Microsoft Corp.*, 224 F. Supp. 2d 76, 86 n.3 (D.D.C. 2002). This group is composed of California, Connecticut, the District of Columbia, Florida, Iowa, Kansas, Massachusetts, Minnesota, Utah, and West Virginia. *Id.*

20. *Microsoft Corp.*, 231 F. Supp. 2d at 149–50.

21. *Massachusetts v. Microsoft Corp.*, 373 F.3d 1199, 1204 (D.C. Cir. 2004).

22. COMMISSION DECISION, *supra* note 1, ¶ 32 (quoting Council Directive 91/250/EEC on the Legal Protection of Computer Programs, 1991 O.J. (L 122) 42).

23. *Id.* ¶¶ 473–514, 541, 779.

24. *Id.* ¶ 779.

25. *Id.* ¶ 543.

“entirety of the circumstances surrounding a specific instance of a refusal to supply.”²⁶ In setting out this standard, the Commission relied on *Volvo v. Veng*, in which a car manufacturer refused to license its product designs so that independent dealers could make spare parts for the manufacturer’s cars.²⁷ The Commission examined Microsoft’s business in the workgroup server market and found interoperability to be a key factor in Microsoft’s success in that market.²⁸

Microsoft, in its defense, put forth three alternatives that would achieve the same effect as licensing interoperability with Windows: (1) the use of open industry standards supported in Windows, (2) the distribution of client-side software, and (3) the possibility of reverse engineering.²⁹ These arguments were summarily rejected by the Commission as simply inaccurate.³⁰ For example, the Commission cited earlier failed attempts at reverse engineering simpler Windows products—even after years of effort and significant investment—by both Sun and IBM.³¹

The idea of reverse engineering software is similar to having a television with over a thousand plugs on the back of it. One may first determine what is capable of plugging into the television and then design a product compatible with that plug. On the other hand, it would be simpler to analyze the inside of the television, find out which wires are associated with a particular function, determine the exterior plug with which it corresponds, and finally design a product that interacts appropriately. Understanding how technology operates internally, as opposed to merely analyzing the outside of the device, saves substantial amounts of time and money when designing a compatible product.

Microsoft then argued that its rights in its intellectual proprietary products should justify maintaining absolute discretion with respect to whom it licenses its product, regardless of antitrust law.³² Despite Microsoft’s zealous response, the Commission rejected this argument for several reasons. First, it reasoned that consumers benefit from more competition in the market.³³ Second, it reasoned that there is a greater possibility of innovation with more competition.³⁴ The Commission concluded that these reasons outweighed Microsoft’s right to unfettered protection of its intellectual property.³⁵ Indeed, the Commission found that the purpose of intellectual property rights is not only to protect a

26. *Id.* ¶¶ 558–559.

27. *Id.* ¶ 557 (citing Case 238/87, *Volvo v. Veng*, 1988 E.C.R. 6211).

28. *Id.* ¶ 637. Microsoft itself has used the argument of interoperability when it sells its products as a superior alternative to the competition. *See id.* ¶¶ 638–646.

29. *Id.* ¶ 667.

30. *Id.* ¶¶ 668–687.

31. *Id.* ¶¶ 454–457, 684.

32. *See id.* ¶¶ 709–712.

33. *Id.* ¶ 694.

34. *Id.* ¶ 700.

35. *Id.* ¶ 729.

creator's right to benefit from his work, but also to stimulate creativity itself, which promotes the public good.³⁶ Thus, the principles underlying intellectual property laws support the court's logic.

The Commission concluded that Microsoft had quickly increased its market share in the workgroup server operating system market to such a dominant position that the elimination of market competition in that market was a very real possibility.³⁷ Therefore, "Microsoft's refusal to supply has the consequence of . . . diminishing consumers' choices by locking them into a homogeneous Microsoft solution," which is a violation of European competition law.³⁸

B. Media Player

The Commission examined Microsoft's practice with WMP and the evolution of WMP's relationship to Windows.³⁹ In a similar manner to the Commission's analysis of interoperability, it defined the relevant market and found Microsoft to be in a dominant position.⁴⁰ The Commission reasoned that WMP had been tied to Windows in an anti-competitive manner to give Microsoft a large competitive advantage in the market for media players.⁴¹ Based on the market research and evidence presented, the Commission found that Microsoft's advantage was due not to having the better product, but rather on the tying of WMP to Windows.⁴² This tying inevitably would lead to barriers to entry for future competition.⁴³ For reasons similar to those cited above for interoperability, the benefits associated with untying WMP, plus the incentives for software innovation and product improvements for Microsoft, existing competitors, and potential competitors, outweighed Microsoft's interest in maintaining the linking of the products.⁴⁴ The Commission also identified the problem posed by the potential leverage that Microsoft would be able to use, facilitating this abusive practice in adjacent software markets.⁴⁵ The Commission concluded that the tying of WMP to Windows was an abuse of its dominant position, thus a violation of European competition law.⁴⁶

36. *Id.* ¶ 711.

37. *Id.* ¶¶ 779–781.

38. *Id.* ¶ 782.

39. *Id.* ¶ 792.

40. *Id.* ¶¶ 471, 799.

41. *Id.* ¶ 979.

42. *Id.* ¶¶ 971–977.

43. *Id.* ¶¶ 416–424.

44. *Id.* ¶ 981.

45. *Id.* ¶ 982.

46. *Id.*

IV. REMEDIES

The Commission separately addressed the two issues— interoperability and tying—and fashioned appropriate remedies for each of the violations. For interoperability and the refusal to supply, the Commission granted the obvious remedy of requiring Microsoft to disclose the specifications necessary for interfacing with its products.⁴⁷ This applied retroactively to programs that Microsoft still supported or marketed,⁴⁸ as well as prospectively to future generations of its products.⁴⁹ The purpose of the Commission’s ruling was to allow companies offering similar products the opportunity to compete effectively with Microsoft’s workgroup server operating system.⁵⁰

For tying, the Commission ordered Microsoft to offer a version of Windows separate from WMP.⁵¹ It was important to the Commission that Microsoft not diminish the performance of the unbundled version of Windows.⁵² Accordingly, the Commission left open the possibility to review the case should that happen.⁵³ The Commission went to lengths to address Microsoft’s argument that Windows cannot be untied from WMP. At trial, however, it was demonstrated that other media players could work effectively on Windows XP Embedded.⁵⁴ Windows XP Embedded is a stripped-down version of Windows that Microsoft markets to operators of smaller devices, such as automatic teller machines.⁵⁵ This stripped-down version can be configured to not include WMP.⁵⁶ Thus, the Commission found Microsoft’s argument that Windows and WMP cannot be separated to be completely without merit.⁵⁷ Furthermore, the Commission cited the U.S. Court of Appeals for the District of Columbia, finding that even if the argument was true, it would not be a justification for anticompetitive behavior.⁵⁸

Last, the Commission ordered two further remedies in this decision. The Commission ordered a Monitoring Trustee to “issue opinions . . . on whether Microsoft has, in a specific instance, failed to comply with this Decision, or on any issue that may be of interest with respect to the effective enforcement of this Decision.”⁵⁹ The Commission also imposed

47. *Id.* ¶ 1004.

48. *Id.* ¶¶ 1000–1001.

49. *Id.* ¶ 1002.

50. *Id.* ¶ 1003.

51. *Id.* ¶ 1011.

52. *Id.* ¶ 1012.

53. *Id.*

54. *See id.* ¶¶ 1018–1021 & n.1279.

55. *Id.* ¶ 1029 & n.1291.

56. *Id.*

57. *Id.* ¶ 1027.

58. *Id.* ¶ 1034 (quoting *United States v. Microsoft Corp.*, 253 F.3d 34, 66 (D.C. Cir. 2001), which found the justification for commingling Internet Explorer code with Windows code an improper justification for anticompetitive behavior).

59. *Id.* ¶ 1045.

a fine, based on the gravity and duration of the infringement, in the amount of €497,196,304.⁶⁰ Microsoft raised three supplemental objections in response to the fine, but the court also rejected these arguments.⁶¹ In doing so, the Commission found that Microsoft had violated parts of European law.⁶² The Commission stated that it was not making new law; instead, it relied on reasonings and holdings of previous decisions, indicating that Microsoft should have been aware of the law.⁶³ It also found that the when the abuse began was irrelevant in deciding whether a fine should be imposed.⁶⁴

It is important to note what the European Court did *not* order. For example, it did not decide that Microsoft must break up into separate companies, with a new independent company for WMP. Also, it did not require Microsoft to divest its interests in any of its products or in any markets. The remedy may be viewed as a less demanding one than may have been imposed initially by the district court in the United States.⁶⁵ Nonetheless, the remedy is more detrimental to Microsoft than the decision by the same district court at a later date.⁶⁶

Microsoft filed its appeal of the case and for a stay of the remedies on June 7, 2004.⁶⁷ These remedies have been stayed by a judge pending Microsoft's appeal of the remedies.⁶⁸ The Court of First Instance will hear Microsoft's case on September 30 and October 1, 2004.⁶⁹ On these dates, the Court will only decide whether or not to continue a stay on the remedies until the final appeal on the substance of the case. The appeal to the European Court of Justice on the substance of the case could take several years.

V. IMPLICATION OF DECISION

A. *Intellectual Property Rights vs. Antitrust Law*

One of the most powerful aspects of the Microsoft litigation was its self-proclaimed battle for all technology companies and their intellectual property rights. The arguments enumerated in the Commission's

60. *See id.* ¶¶ 1059–1078 (explaining the methods for determining the amount of the fine in question). As noted in Section I, the fine was the equivalent of roughly \$635 million.

61. *Id.* ¶ 1057.

62. *Id.* ¶¶ 1056–1057.

63. *Id.*

64. *Id.*

65. *See United States v. Microsoft Corp.*, 87 F. Supp. 2d 30, 37–54 (D.D.C. 2000).

66. *See United States v. Microsoft Corp.*, 231 F. Supp. 2d 144, 149–50 (D.D.C. 2002).

67. Action Brought on 7 June 2004 by Microsoft Corporation against the Commission of the European Communities, 2004 O.J. (C 179) 18, 19.

68. *Microsoft Corp.: Date is Set for EU Court to Hear Appeal of Ruling*, WALL ST. J., July 28, 2004, at C14.

69. *Id.*

decision have been raised again in Microsoft's appeal⁷⁰ and its press release, which details its view of the implications of the decision for all other technology companies.⁷¹ Despite the vigor with which Microsoft promotes its views on the supremacy of intellectual property, they have not been met with great approval.

The tension between intellectual property rights and antitrust law has been explored in numerous law review articles.⁷² Some authors have suggested a balancing test between incentives for inventors and competition in the marketplace,⁷³ while others have suggested a rule of reason standard for refusals to deal.⁷⁴ For the Microsoft case, the European Commission adopted a balancing test for analyzing the issues in question.⁷⁵ In contrast, the U.S. Department of Justice has long advocated a rule of reason test.⁷⁶

B. Microsoft's View

Microsoft has not indicated approval of either test. One may think it would endorse the Department of Justice's standard, if only because the U.S. court followed the rule of reason view and ruled in Microsoft's favor. Microsoft believes that, on balance, its intellectual property rights are more important than the benefit of competition to consumers. It also sees the protection of its products as reasonably related to the best interest of the public.⁷⁷ Microsoft emphasizes that the European Court was wrong for a variety of reasons under the balancing test.⁷⁸ Yet, the U.S. district court,⁷⁹ the U.S. Circuit Court of Appeals,⁸⁰ and the European Commission all rejected Microsoft's arguments of the

70. Action Brought on 7 June 2004 by Microsoft Corporation against the Commission of the European Communities, 2004 O.J. (C 179) 18, 19.

71. Press Release, Microsoft Corp., The European Commission's Decision in the Microsoft Case and Its Implications for Other Companies and Industries (April 2004), at <http://download.microsoft.com/download/5/2/7/52794f65-8784-43cf-8651-c7d9e7d34f90/Comment%20on%20EC%20%20Microsoft%20Decision.pdf> [hereinafter Microsoft Press Release].

72. See, e.g., Simon Genevaz, *Against Immunity for Unilateral Refusals to Deal in Intellectual Property: Why Antitrust Law Should Not Distinguish Between IP and Other Property Rights*, 19 BERKELEY TECH. L.J. 741 (2004); Daniel J. Gifford, *Antitrust's Troubled Relations with Intellectual Property*, 87 MINN. L. REV. 1695 (2003); Robert Pitofsky, *Antitrust and Intellectual Property: Unresolved Issues at the Heart of the New Economy*, 16 BERKELEY TECH. L.J. 535 (2001); Seungwoo Son, *Selective Refusals to Sell Patented Goods: The Relationship Between Patent Rights and Antitrust Law*, 2002 U. ILL. J.L. TECH. & POL'Y 109.

73. See, e.g., Son, *supra* note 72, at 190.

74. See, e.g., Genevaz, *supra* note 72, at 741.

75. COMMISSION DECISION, *supra* note 1, ¶¶ 558, 783; see also Microsoft Press Release, *supra* note 71, at 2 (denouncing the Commission's "new balancing test").

76. FEDERAL TRADE COMMISSION & U.S. DEP'T OF JUSTICE, ANTITRUST GUIDELINES FOR THE LICENSING OF INTELLECTUAL PROPERTY 21-22 (Apr. 6, 1995), available at <http://www.usdoj.gov/atr/public/guidelines/ipguide.pdf>.

77. See generally COMMISSION DECISION, *supra* note 1.

78. Microsoft Press Release, *supra* note 71, at 2.

79. *United States v. Microsoft Corp.*, 87 F. Supp. 2d 30, 40-41 (D.D.C. 2000).

80. *United States v. Microsoft Corp.*, 253 F.3d 34, 63 (D.C. Cir. 2001) (per curiam).

superiority of intellectual property rights as compared to antitrust laws.⁸¹ Apparently, the public benefits of antitrust law actually outweigh the private benefits of Microsoft's intellectual property rights.⁸²

Given the weakness of Microsoft's arguments and the previous unfavorable decisions, it is difficult to imagine the European Court of Justice ruling favorably for Microsoft. Nevertheless, given the length of time likely to transpire before an ultimate conclusion, it is difficult to state with any certainty what changes may take place in the markets, European law, and practices by Microsoft that could potentially affect the final decision.

VI. CONCLUSION

The European Commission's decision has set forth important limitations on intellectual property rights when in conflict with European competition law. The full ramifications of the decision are impossible to determine until the appeals process closes its first chapter in October 2004. The courts on both sides of the Atlantic agree that some of Microsoft's business practices ran afoul of antitrust law, but the remedies chosen by each court were quite different. It will take a few years to appreciate which remedy is most effective. The majority of the commission's findings likely will be upheld, but some parts of the remedies, namely the separation of WMP from Windows, may not be accepted by the higher courts.

81. COMMISSION DECISION, *supra* note 1, ¶ 729.

82. *See, e.g., id.* ¶¶ 186–195.