

IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF COLUMBIA

STATE OF NEW YORK *ex. rel.*
Attorney General ELIOT SPITZER, *et al.*,

Plaintiffs,

v.

MICROSOFT CORPORATION,

Defendant.

Civil Action No. 98-1233 (CKK)

EXECUTIVE SUMMARY OF DIRECT TESTIMONY OF BILL GATES

Bill Gates is the Chairman of the Board and Chief Software Architect of Microsoft. He co-founded Microsoft in 1975 together with his friend Paul Allen. Mr. Gates was Microsoft's Chief Executive Officer from 1986, when the company went public, until January 2000. Mr. Gates relinquished his duties as CEO in January 2000 so that he could spend more time working with the product groups at Microsoft to develop new technologies that will be necessary to enable the next generation of computing.

Mr. Gates is submitting testimony in this action to provide the Court with information concerning Microsoft's development of platform technology and how OEMs, ISVs and others use that technology in building new products. Mr. Gates also describes his belief that Microsoft has made a significant contribution to the success of the PC industry through its development and broad licensing of the Windows family of desktop operating systems, as well as other popular software products.

In his testimony, Mr. Gates identifies the key elements of Microsoft's business model that have been essential to the success of Windows and, more importantly, to the value

Windows has provided to the marketplace. He then explains why the non-settling States' proposed remedy would deprive the marketplace of the primary benefits provided by Windows, resulting in great harm to the PC ecosystem and to consumers.

In fact, Mr. Gates explains why Microsoft would be unable to develop a version of Windows that would comply with Section 1 of the non-settling States' proposed remedy. Section 1 thus would ban Microsoft from continuing to license its Windows desktop operating systems six months after entry of the non-settling States' proposed remedy, unless the Court later agreed to modify the provision.

Mr. Gates's testimony is divided into three sections. In Section I, Mr. Gates describes Microsoft's formation and its early development of operating system products. As Mr. Gates explains, for more than 25 years, Microsoft has been at the forefront of the development of the PC industry. In particular, Microsoft's creation and nurturing of a common software platform that ran across multiple brands of PCs—namely, Microsoft's MS-DOS and later Windows operating systems—helped to unify a fragmented industry. Microsoft's platform software provided consumers with the benefits of broad interoperability across (i) PCs from many different OEMs and (ii) applications from many different ISVs. It is no exaggeration to say that Microsoft helped to bring about a revolution in computing.

Mr. Gates also briefly describes in Section I of his testimony Microsoft's current efforts via its .NET and Trustworthy Computing initiatives to develop breakthrough technologies that, if successful, could spark a new round of investment and excitement in computing. For example, Microsoft today is investing heavily in XML Web Services, a next-generation computing platform that holds the potential to unleash new waves of productivity gains in the economy.

In Section II of his testimony, Mr. Gates addresses three overarching elements of Microsoft's business model that have contributed significantly to Microsoft's success and to the success of every other company that builds products that take advantage of the Windows platform. Those three elements are: (i) the stability, consistency and quality of Windows and Microsoft's commitment to developing new releases of the operating system that provide ISVs and consumers with new innovative features and functionality; (ii) the interoperability across a wide range of hardware and software that Windows provides; and (iii) the central role played by intellectual property protection in providing Microsoft with an incentive to invest capital, time and energy in developing new software. The non-settling States' proposed remedy would undermine all three of these elements, causing great damage to Microsoft, other companies that build on Microsoft's platforms, and consumers of PC software.

In Section III of his testimony, Mr. Gates analyzes each of the substantive provisions of the non-settling States' proposed remedy on a section-by-section basis. Mr. Gates explains why the non-settling States' proposed remedy would result in the fragmentation of the Windows platform. This fragmentation would harm not just Microsoft, but also the many other companies that have built products and businesses based on the stable and evolving Windows platform, as well as all Windows users. The only companies that would arguably benefit from the fragmentation of the Windows platform are Microsoft's competitors.

Mr. Gates then explains why the non-settling States' proposed remedy would deprive Microsoft of much of the economic value of its two most important products, Windows and Office. In fact, if entered by the Court, the non-settling States' proposed remedy would result in a massive transfer of Microsoft's present and future intellectual property rights in Windows and Office to Microsoft's competitors. With free access to Microsoft's technology,

competitors could build a clone of Windows (a product that mimics the key features of the operating system) and their own version of Office without bearing any significant part of the R&D expenses that Microsoft incurred to build the technology. Indeed, providing Microsoft's technology to its competitors to enable them to build "functional equivalents" of Microsoft's products appears to be a central objective of the non-settling States' proposed remedy.

Mr. Gates testifies that the non-settling States' proposed remedy would greatly reduce Microsoft's incentive and ability to develop and deliver new technologies to the marketplace. The non-settling States' proposed remedy thus would have three consequences.

First, companies that build on or otherwise benefit from Microsoft's heavy investment in developing new technologies—OEMs, ISVs and the businesses and individual consumers who use Microsoft's software—would be harmed. With the loss of the positive feedback benefits provided by Windows, the marketplace would experience higher prices and less innovation.

Second, the non-settling States' proposed remedy would prevent Microsoft from delivering breakthrough technologies, such as its current .NET initiative, that will be necessary to enable the next-generation of computing. This would have a significant adverse impact on companies that are building businesses on .NET and on consumers who would be denied the benefits of the new and exciting innovations .NET promises to deliver. Microsoft's market capitalization is based on the market's well-founded belief that Microsoft is on a path to deliver a wide range of those breakthrough technologies, which will generate new sources of revenue. Microsoft thus would be greatly devalued as a company if the non-settling States' proposed remedy were entered.

Third, competition would be reduced not only in operating systems, but also in other key product categories where Microsoft is the strongest challenger to incumbent leaders. These categories include online services (where AOL Time Warner leads), handheld devices (where Palm leads) and game consoles (where Sony leads). Indeed, in the important area of server computing—both hardware and software—the strongest competitive challenge to incumbent, high-priced UNIX vendors such as Sun Microsystems is the PC model. Under this model, multiple OEMs building on a standard, widely licensed and attractively priced operating system, such as Windows 2000 Server, compete, resulting in lower prices for consumers.

Finally, Mr. Gates explains in Section III of his testimony why it would be extremely difficult, if not impossible in some cases, for Microsoft to comply with the non-settling States' proposed remedy as written. Many provisions of the non-settling States' proposed remedy, particularly its definitions relating to "middleware," are vague and ambiguous. As such, they do not provide Microsoft with a clear statement of its obligations. Other provisions of the non-settling States' proposed remedy are simply not feasible to implement. Although many provisions would lead to extreme results, Microsoft would not have the freedom to construe the non-settling States' proposed remedy in ways that it finds less extreme.

As Mr. Gates explains, Microsoft is committed to complying fully with Court orders, including any remedy that may be ordered in this case. Microsoft can do so, however, only if the remedy is clear as written and it is technically feasible to comply with its terms. Any remedy imposed also should preserve the economic and consumer benefits that Windows provides and maintain Microsoft's incentive to bring new innovations to the marketplace.