2007

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NOTE

MICROSOFT TYING CONSUMERS' HANDS? THE WINDOWS VISTA PROBLEM AND THE SOUTH KOREAN SOLUTION

By Daniel J. Silverthorn*

On January 30, 2007, after five years of development and a budget of over $6 billion, the Microsoft Corporation released Windows Vista to the public.[1] Windows Vista is the latest edition of the Windows operating system for personal computers (PCs). Windows accounts for thirty percent of Microsoft's $44 billion in sales and sixty percent of its operating profit.[2] Estimates show that $70 billion in products and services revolving around Windows Vista will be sold in 2007 alone,[3] and that Windows Vista will be installed on more than half of the world's consumer PCs by late 2008.[4] Steven A. Ballmer, the company's chief executive, called Vista "the biggest product launch in Microsoft's history."[5]

However, accusations of antitrust violations have surrounded Microsoft and its new operating system. Currently, more than ninety percent of

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1.   Daisuke Wakabayashi, *Vista is Ready for Consumers but Businesses Key*, WASHINGTON POST, Jan. 29, 2007, *available at* http://www.washingtonpost.com/wp-dyn/content/article/2007/01/29/AR2007012900498.html (last visited Feb. 17, 2007).

2.   *Id.*

3.   Steve Lohr, *First the Wait for Microsoft Vista; Now the Marketing Barrage*, N.Y. TIMES, Jan. 30, 2007, at C1.

4.   Wakabayashi, *supra* note 1.

5.   Lohr, *supra* note 3.

the world's PCs operate under Windows.[6] To cement its market power, Microsoft has engaged in controversial business practices. Those practices have led to adverse antitrust decisions in the United States, the European Union (EU), and South Korea. Many of these decisions, both judicial and administrative, revolve around Microsoft's bundling, or "tying," of certain subsidiary applications with the Windows operating system, including Internet Explorer and Windows Media Player. In doing so, Microsoft arguably gains a greater than deserved market share with these bundled applications, inhibiting fair competition in the software marketplace. The United States, EU and South Korean antitrust decisions addressing this tying of software have each produced different outcomes in their respective jurisdictions.

This Note analyzes Microsoft's newest operating system, Windows Vista, by focusing on the tying aspect of antitrust law using the precedent set by those three jurisdictions. Part I discusses the recent Microsoft antitrust litigation and settlement in the United States, the European Commission's ruling against Microsoft in the EU and the Korea Fair Trade Commission's decision against Microsoft in South Korea. Part II explains why South Korea took the most appropriate approach to opening competition for non-Microsoft applications, a method compatible with current U.S. law governing antitrust tying arrangements under the Sherman Act. Part III examines Windows Vista and its multitude of tied or bundled applications, concluding that a South Korean-type approach to Windows Vista would successfully limit Microsoft's unfair advantage in tied applications.

PART I

A. *Microsoft Windows*

Operating systems serve as the backbone of personal computers. An operating system provides a graphical interface for user interaction with the PC, and it performs such tasks as allocating computer memory and controlling input and output peripherals.[7] Operating systems also function as platforms for software applications.[8] Given that Microsoft Windows has enjoyed a near-monopoly in the operating system market since the early-to-mid 1990s, the vast majority of software applications are specifically designed to work with Windows.

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6.   *Id.*
7.   U.S. v. Microsoft Corp., 253 F.3d 34, 53 (D.C. Cir. 2001).
8.   *Id.*

Microsoft also bundles various software applications with its operating system, such as the Internet Explorer web browser and Windows Media Player. The bundling of this software with Windows quickly invokes accusations of antitrust violations. Accusers claim that Microsoft's practices raise entry barriers to certain software markets, restricting free competition and impeding consumer welfare. Because of this and other allegedly anticompetitive business practices, Microsoft has faced antitrust lawsuits and sanctions in the United States, the EU and South Korea.

B. *United States v. Microsoft*

In 1998, the United States, nineteen individual states, and the District of Columbia brought consolidated civil enforcement actions against Microsoft under the Sherman Antitrust Act.[9] The plaintiffs identified four distinct violations of the Sherman Act, one being a tying arrangement of unlawfully bundling the Internet Explorer Web browser software application with the Windows 95 and Windows 98 PC operating systems in violation of Section 1 of the Sherman Act. A tying arrangement is "an agreement by a party to sell one product but only on the condition that the buyer also purchases a different (or tied) product, or at least agrees that he will not purchase that product from any other supplier."[10] A tying arrangement violates Section 1 of the Sherman Act if "the seller has 'appreciable economic power' in the tying product market and if the arrangement affects a substantial volume of commerce in the tied market."[11] The plaintiffs also charged Microsoft with violating various state antitrust laws.[12]

In 2000, the U.S. District Court for the District of Columbia found that Microsoft violated the Sherman Act by illegally tying its operating system and Internet Explorer, among other federal antitrust violations. The District Court also concluded that its ruling on those federal law claims "satisfie[d] the elements of analogous causes of action arising under the laws of each particular state."[13] Microsoft immediately appealed.

On appeal, the U.S. Court of Appeals for the District of Columbia Circuit disagreed with the lower court's use of a "per se" rule for the

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9.   U.S. v. Microsoft Corp., 87 F.Supp.2d 30, 35 (D.D.C. 2000).

10.   Eastman Kodak Co. v. Image Tech. Servs., 504 U.S. 451, 461 (1992), (citing Northern Pacific R. Co. v. U.S., 356 U.S. 1, 5–6 (1958)).

11.   Eastman Kodak Co., 504 U.S. at 462 (citing Fortner Enterprises, Inc. v. U.S. Steel Corp., 394 U.S. 495, 503 (1969)).

12.   *Microsoft*, 87 F.Supp.2d at 35.

13.   *Id.*

tying of an operating system and a software application.[14] The Court of Appeals instead decided that the lower court should analyze a software bundling case under the far more flexible rule of reason.[15] According to the court, this rule of reason "more freely permits consideration of the benefits of bundling in software markets, particularly those for [operating systems], and a balancing of these benefits against the costs to consumers whose ability to make direct price/quality tradeoffs in the tied market may have been impaired."[16] The Court of Appeals then remanded the case to the District Court to reconsider, among other issues, the tying inquiry under the rule of reason.[17]

However, before the District Court could rule on remand, the United States, Microsoft, and 9 of the 20 state plaintiffs agreed to a proposed settlement.[18] District Court Judge Kollar-Kotelly delivered a judgment which essentially adopted this settlement, and rejected the other states' proposed remedies.[19] However, this settlement did not include a remedy for the tying claim.[20] Since the tying claim was not pursued on remand, there was no finding of liability on which to base the remedy.[21] In 2004, the Court of Appeals for the D.C. Circuit upheld the District Court's judgment in its entirety.[22]

Among the many restrictions of the settlement, Microsoft was prohibited from restricting a PC original equipment manufacturer from installing and promoting third-party applications.[23] Yet the settlement did not force Microsoft to remove any of its applications from Windows.[24]

C. European Union

On March 24, 2004, the European Commission (the executive body of the EU) ruled that the inclusion of Windows Media Player with Windows violated the antitrust provisions of Article 82 of the EC Treaty.[25]

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14.   *Microsoft*, 253 F.3d at 84.

15.   *Id.*

16.   *Id.* at 94.

17.   *Id.*

18.   Andrew Chin, *Decoding Microsoft: A First Principles Approach*, 40 WAKE FOREST L. REV. 1, 65 (2005).

19.   *Id.*

20.   *Id.* at 73.

21.   *Id.*

22.   *Id.* at 76.

23.   Final Judgment at 3, U.S. v. Microsoft Corp., Civil Action No. 98-1232 (D.D.C. Nov. 12, 2002), http://www.usdoj.gov/atr/cases/f200400/200457.pdf (last visited Feb. 19, 2007).

24.   Chin, *supra* note 18, at 74.

25.   Treaty Establishing the European Community, art. 82, 2006 O.J. (C 321) 1, http://eur-lex.europa.eu/LexUriServ/site/en/oj/2006/ce321/ce32120061229en00010331.pdf (last visited Feb. 15, 2007).

Even though the U.S. settlement provided that Microsoft should allow computer manufacturers and consumers to enable or remove end-user access to Microsoft applications, the Commission found this remedy insufficient and ordered Microsoft to market a version of Windows that did not include Windows Media Player.[26] The Commission also found antitrust violations under Microsoft's work group server operating systems[27] (this Note does not discuss the server versions of Windows, which are different from the Windows operating systems for PCs).

In total, the Commission forced Microsoft to pay a fine of over 497 million Euros (about $613 million).[28] Microsoft is currently appealing the decision before the EU Court of First Instance in Luxembourg.[29] Bo Vesterdorf, the president of the EU Court of First Instance, hopes to issue a ruling on Microsoft's appeal by the time he leaves office in September 2007.[30]

D. *South Korea*

In December 2005, the Korea Fair Trade Commission fined Microsoft 33 billion Won (approximately $32 million) for abuse of its

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Article 82 of the EC Treaty states:

Any abuse by one or more undertakings of a dominant position within the common market or in a substantial part of it shall be prohibited as incompatible with the common market insofar as it may affect trade between Member States.

Such abuse may, in particular, consist in:
(a) directly or indirectly imposing unfair purchase or selling prices or other unfair trading conditions;

(b) limiting production, markets or technical development to the prejudice of consumers;

(c) applying dissimilar conditions to equivalent transactions with other trading parties, thereby placing them at a competitive disadvantage;

(d) making the conclusion of contracts subject to acceptance by the other parties of supplementary obligations which, by their nature or according to commercial usage, have no connection with the subject of such contracts.

26.   Commission of the European Communities, Commission Decision of 24.03.04 relating to a proceeding under Article 82 of the EC Treaty (Case COMP/C-3/37.792 Microsoft), 2004 O.J. (C900), *available at* http://ec.europa.eu/comm/competition/antitrust/cases/decisions/37792/en.pdf (last visited Feb. 19, 2007) [hereinafter Commission Decision].

27.   CNET Staff, *EU's statement on end of Microsoft investigation*, CNET NEWS.COM, March 24, 2004, http://news.com.com/EUs+statement+on+end+of+Microsoft+investigation/2100-1014_3-5178465.html (last visited Feb. 19, 2007).

28.   Associated Press, *EU Microsoft judge: ruling by September*, BOSTON HERALD, Feb. 5, 2007, *available at* http://business.bostonherald.com/technologyNews/view.bg?articleid=181231.

29.   *Id.*

30.   *Id.*

market-dominant position.[31] The Commission ruled that Microsoft had violated South Korea's Monopoly Regulation and Fair Trade Act by bundling Windows Media Player and Windows Messenger with Windows.[32] The ruling pointed to Microsoft's large gain in market share once both media player and instant messaging software were bundled with Windows; the ruling also acknowledged that Microsoft's market share gain translated into a large market share drop for competing software.[33]

South Korea then went further than either the United States or the EU. In addition to the fine, the Korea Fair Trade Commission ordered Microsoft to market two versions of Windows. The first version would be stripped of Windows Media Player and Windows Messenger, while the second version would include both software applications, but would also direct users to Web pages where they could download competing software.[34]

PART II

Microsoft claims that its bundled versions of Windows benefit both consumers and the technology industry.[35] The company argues that the bundled versions do not block competition because software developers can successfully distribute their software to end users, and these end users can easily choose to install and utilize that software.[36] However, despite Microsoft's assurances, significant barriers exist for software applications that wish to integrate into Windows.

When a software company decides to create a web browser, media player, or other software application, it must expend a large amount of capital attempting to compete with existing software, including Microsoft's software. A large software company can conceivably do this. However, since Microsoft bundles its software with Windows, the vast majority of personal computers already include Microsoft software. Any

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31.   The findings of the Korea Fair Trade Commission can be found at http://ftc.go.kr/data/hwp/micorsoft_case.pdf. *See also* Aaron Tan, *South Korea fines Microsoft $32 Million*, ZDNET, Dec. 7, 2005, http://news.zdnet.com/2100-3513_22-5985332.html (last visited Feb. 19, 2007).

32.   *Id.* The Commission also found a violation for Microsoft bundling Windows Media Service with server versions of Windows, *Id.*

33.   *Id.*

34.   *Id.*

35.   CBS/AP, *Microsoft-EU Antitrust Talks Fail*, CBS NEWS, March 18, 2004, http://www.cbsnews.com/stories/2003/09/26/tech/main575412.shtml (last visited Feb. 16, 2007).

36.   Press Release from Microsoft, Microsoft Submits Proposed Findings of Fact, Aug. 10, 1999, http://www.microsoft.com/presspass/features/1999/08-10findings.mspx (last visited Feb. 14, 2007).

company that wishes to compete with Microsoft faces a seemingly endless uphill battle to claim any remaining market share from the Windows-bundled applications. Entry barriers result for these software companies.

For example, in the EU ruling, the European Commission found tremendous growth in Windows Media Player market share once it was included in Windows.[37] In October 1999, immediately before Microsoft began including Windows Media Player with its operating system, 50% of users reported that the media player they used most often was RealNetworks' RealPlayer.[38] By August 2003 this figure had fallen to 19%.[39] In that same period Windows Media Player's share increased significantly from 22% to 45%.[40] The EU further found that tying Windows Media Player to Windows discouraged computer manufacturers from shipping personal computers with non-Microsoft media players preinstalled. In fact, RealNetworks had to pay computer manufacturers to preinstall its software in order to promote product usage.

South Korea's decision, more so than the U.S. settlement and the EU ruling, will assist companies like RealNetworks. By forcing Microsoft to provide the two versions of Windows, South Korea removes some of the competition barriers created by Microsoft's bundling. In addition, even the versions of Windows that include bundled Microsoft applications point users to online lists of competing software, allowing consumers to make an informed decision as to choice of application. As more competitors enter the market, Microsoft will have a stronger incentive to produce better software applications to encourage Windows users to choose Microsoft's application over the competitors' application.

On the other hand, the U.S. solution has proven untenable. As a result of the U.S. settlement and judgment, Microsoft must allow computer manufacturers to remove default access to Microsoft applications and install third-party programs as the default program. However, the Microsoft application remains installed on the computer, immediately available to the user. Even more problematic, few computer manufacturers have chosen to change the default applications, realizing that consumers are less likely to buy computers if they are unfamiliar with the default software.

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37.   Commission of the European Communities, Commission Decision of 24.03.04 relating to a proceeding under Article 82 of the EC Treaty (Case COMP/C-3/37.792 Microsoft), 2004 O.J. (C900), *available at* http://ec.europa.eu/comm/competition/antitrust/cases/decisions/37792/en.pdf.

38.   *Id.*

39.   *Id.*

40.   *Id.*

Some claim that remedies such as those adopted by the EU and South Korea impose significant costs on consumers without any incremental competitive benefit.[41] Others argue that non-Microsoft software developers need Microsoft's software interfaces (known as APIs) into Windows to better create Windows-compatible applications.[42]

However, the EU case demonstrates that Microsoft could remove the tied software while allowing the APIs to remain. The EU instructed Microsoft to remove Windows Media Player from Microsoft Windows but allowed Microsoft to keep the APIs for other applications to use. The European Commission specifically requested that no reduction in performance should result. Microsoft then successfully distributed an alternative version of Windows for the EU market place, known as Windows XP N (and later Windows Vista N) which did not include Windows Media Player. If Microsoft successfully achieved this with Windows Media Player, then it should be able to do the same with other applications, given its strong supply of developers, engineers, and resources.

Despite the South Korean approach, recent domestic developments suggest that the settlement between the U.S. government and Microsoft will remain. According to J. Bruce McDonald, deputy assistant attorney general in the Justice Department's antitrust division, the South Korean remedy "goes beyond what is necessary or appropriate to protect consumers, as it requires the removal of products that consumers may prefer."[43] Moreover, in late 2006, the *United States v. Microsoft* plaintiffs and Microsoft issued a joint status report on Microsoft's compliance with the final judgments, as required under the settlement.[44] The report stated that Windows Vista satisfied the terms of the settlement and did not appear to raise antitrust concerns.[45] However, the District Court never made a final decision on the tying claim under the Sherman Act as the settlement occurred before the court could rule on remand. If the litigation were to return to court with Windows Vista at the center of the controversy, the outcome could mimic the original District Court deci-

41.   David S. Evans, Albert L. Nichols, & Richard Schmalensee, *United States v. Microsoft: Did Consumers Win?* 1 J. COMPETITION L. & ECON. 497, 501 (2005).

42.   Written Direct Testimony of Christopher Jones, N.Y. v. Microsoft, No. 98-1233 (D.C.C. April 25, 2002), http://www.microsoft.com/presspass/legal/jones.mspx (last visited Mar. 7, 2007).

43.   Declan McCullagh, *Feds side with Microsoft in Korea flap*, ZDNET, Dec. 7, 2005, http://news.zdnet.com/2100-3513_22-5985912.html (last visited Feb. 13, 2007).

44.   Joint Status Report on Microsoft's Compliance with the Final Judgments, United States v. Microsoft Corp., Civil Action No. 98-1232 (D.D.C. Nov. 21, 2006),
      http://www.usdoj.gov/atr/cases/f219800/219800.pdf (last visited Feb. 13, 2007).

45.   *Id. See also* Anne Broache, *Justice Dept.: Vista satisfies antitrust deal*, CNET NEWS.COM, Nov. 21, 2006, http://news.com.com/Justice+Dept.+Vista+satisfies+antitrust+deal/2100-1016_3-6137603.html (last visited Feb. 16, 2007).

sion with the court ruling that the tying of software applications to the operating system would violate Section 1 of the Sherman Act.

PART III

Microsoft included numerous new applications with Windows Vista. All editions are bundled with Internet Explorer 7, Windows Media Player 11, Windows Mail e-mail client, Windows Calendar, Windows Photo Gallery, Windows Sync Center for mobile devices, Windows Mobility Center for presentations on the road, Windows Security Center, Windows Meeting Space for ad hoc wireless meetings, and Remote Desktop for working from home.[46] Not only is each of these applications bundled with the operating system, each is preferred by the operating system. A CNET review of Windows Vista stated that "the extensive tie-ins to Microsoft.com and Live.com, and the many, many interdependences upon Internet Explorer 7 left us desperately wanting more (and often best-of-breed) alternatives."[47] For example, CNET found that RSS feeds from Internet Explorer 7 get preferential treatment, even though many users prefer to use Firefox or other web browsers.[48]

In a new civil action against Windows Vista, a court could use the rule of reason under antitrust law, with guidance from the EU decision and the South Korean decision, and find that Microsoft's bundling violates the Sherman Act's prohibition against tying arrangements. The court would then have to decide which applications to unbundle from Windows Vista. For example, the *Microsoft* Court of Appeals greatly emphasized Internet Explorer's integration into Windows, stating that this integration needed to remain to appease third party developers.[49] Microsoft applications such as Internet Explorer could not be easily removed without breaking the interdependencies and thus should not be unbundled.[50]

However, when the EU instructed Microsoft to remove Windows Media Player from Microsoft Windows, it allowed Microsoft to keep the APIs used by Windows Media Player for other applications to use, thus not breaking any interdepenancies.[51] The European Commission specifically

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46.   Robert Vamosi, *Microsoft Vista Home Basic*, CNET, Jan. 24, 2007, http:// reviews.cnet.com/Microsoft_Vista_Home_Basic/4505-3672_7-32013641.html (last visited Feb. 16, 2007).

47.   *Id.*

48.   *Id.*

49.   *See* Microsoft Corp., 253 F.3d at 93–94.

50.   *Id.*

51.   Commission Decision, *supra* note 26.

requested that no reduction in performance should occur.[52] Microsoft then successfully distributed Windows XP N and Windows Vista N for the EU marketplace, neither of which includes Windows Media Player.[53] The U.S. plaintiffs could argue that since Microsoft successfully separated Windows Media Player from Windows Vista in Europe, Microsoft could achieve the same result with American versions of Windows Media Player and other Windows Vista applications.

An unbundling of Windows Vista would help Microsoft's competition, but would it help consumers?[54] Many Windows users would finally be introduced to the viable alternatives to Microsoft applications that exist, such as Firefox for Internet Explorer and iTunes for Windows Media Player. There are a host of substitutes for the other applications that Microsoft currently includes in Windows Vista. Most importantly, Microsoft has already carried out an untying remedy in the EU and South Korea, proving that it can be done. Furthermore, any consumer who desired the Microsoft versions of the Windows Vista applications could simply download or purchase them in the same way other software is acquired.

U.S. implementation of the South Korean remedy would force Microsoft to market two versions of every version of Windows Vista. One version of Vista could have Microsoft applications absent, but include a web page link or similar information page with a list of Microsoft software options available for download. The second version of Vista could include all the installed Microsoft applications, but would more prominently display the alternatives available to the user, as quickly as possible after first use. The South Korean solution aligns with the original District Court decision, encourages greater competition and innovation, and as the next plaintiffs should argue, is an antitrust remedy not unduly burdensome for Microsoft.

CONCLUSION

Over the past twenty years, Microsoft has successfully executed a marketing plan that centered on quickly eliminating any real PC operating system competition. At the same time, Microsoft slowly occupied the

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52.   *Id.*
53.   Ina Fried, *Microsoft to Rename Media-Player-Less Windows*, CNET NEWS.COM, March 28, 2005, http://news.com.com/Microsoft+to+rename+media-player-less+Windows/ 2100-1014_3-5643117.html (last visited March 26, 2007).; Ina Fried, *Microsoft Boxes Up Vista*, Feb. 26, 2006, CNET NEWS.COM, http://news.com.com/Microsoft+boxes+up+Vista+- +page+2/2100-1016_3-6043222-2.html?tag=st.num (last visited March 26, 2007).
54.   *See* Evans, *supra* note 41, at 499–500.

field in application software compatible with its operating system, such as internet browsers, media players, and instant messenger services.

The U.S. solution to Microsoft's business practices has resulted in a complete union of operating system and application software. Furthermore, it has created an artificial limitation on the computer manufacturers who now lack the ability to give their customers a choice in application software. By effectively requiring that each user of the operating system have Microsoft applications installed, Windows Vista continues Microsoft's well-known monopolistic approach by reducing competition, raising entry barriers, and inhibiting consumer choice.

In contrast, the South Korean solution to Microsoft's business practices solves many market share issues by forcing Microsoft to develop two versions of its software, and informing users of the choice in software that they have. This Note has argued that the United States should follow South Korea's example if a Windows Vista antitrust lawsuit were to occur (despite the current terms of the *United States v. Microsoft* settlement). If given a meaningful choice, consumers would finally reclaim control of the software marketplace from the hands of the Microsoft and Windows Vista.