Nothing New under the Sun? A Slightly Contrarian Reading of the CFI's *Microsoft* Judgment

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The judgment of the European Court of First Instance (CFI) of 17 September 2007 in the Microsoft case[1] was likely the most eagerly-awaited competition law ruling in EC history. The judgment has given rise to much hyperbole in the media and unprecedented public criticism of the second highest EC court by a foreign government agency.[2]

On closer analysis, the judgment is less remarkable than the circumstances surrounding it. The CFI's judgment very much turns on the specific facts of the case, and makes little if any new law under Article 82 EC. The judgment may well encourage the Commission to act on other pending complaints against Microsoft. But it is unlikely to have any direct bearing on other pending Article 82 EC cases in the technology area. The judgment's most significant, and perhaps least anticipated, practical implications may lie in a completely different area — the use of monitoring trustees in competition cases.

Background

The 2004 Decision. In its decision of 24 March 2004 (the 2004 Decision)[3] the Commission found that Microsoft had infringed Article 82 EC in two ways.

First, the Commission determined that Microsoft had abused its dominant position in the client (PC) operating systems (OS) market and the work group server (WGS) OS market (i.e., file, print, group and user administration services) by refusing to supply indispensable interoperability information to Microsoft's competitors. The interoperability information consisted of protocols necessary for communications between servers and between servers and PCs. The Commission found that Microsoft's refusal to supply this information foreclosed competitors from the server OS market.

Second, the Commission found that Microsoft had infringed Article 82 EC by bundling its Windows Media Player (WMP) with its dominant Windows PC OS. Given the ubiquity of Microsoft's OS, suppliers of other media players could not gain comparable access to consumers' PCs through Internet downloads or installation agreements with original equipment manufacturers (OEM). In assessing foreclosure effects from Microsoft's bundling, the Commission analyzed the incentives for programmers and content developers to focus exclusively on the WMP format, as well as the

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actual growth of WMP's share to the detriment of competing formats.

The Commission ordered Microsoft to remedy these infringements by (a) supplying interoperability information on reasonable and non-discriminatory terms to companies interested in developing WGS OS products (the Interoperability Remedy); and (b) making available a version of its OS that does not include WMP code (the Unbundling Remedy). Additionally, the Commission imposed a fine of €497.2 million and required appointment of a monitoring trustee to supervise the implementation of the remedies.

Subsequent events. Microsoft appealed the 2004 Decision to the CFI. It also sought to stay the implementation of the remedies through an interim measures application, which the CFI President rejected in his Order of 22 December 2004.[4] Thereafter, Microsoft implemented the Unbundling Remedy; but Microsoft is still at loggerheads with the Commission about implementation of the Interoperability Remedy. No fewer than four remedies enforcement proceedings are currently at various procedural stages: (i) Microsoft's appeal of the Commission's €280.5 million July 2005 fining decision for Microsoft's continued failure to make available complete and accurate interoperability information; (ii) the pending administrative proceedings in which the Commission will need to determine whether Microsoft has now fully complied with its obligations to disclose interoperability information; (iii) a separate Commission remedies enforcement proceeding concerning Microsoft's proposed pricing for licenses to its interoperability information; and (iv) an appeal that Microsoft filed in August 2005 against a letter in which the Director-General of DG Competition, Philip Lowe, reminded Microsoft that (if the CFI upheld the 2004 Decision) Microsoft will also have to disclose interoperability information to open source software developers.

The CFI's Judgment

Most experts predicted the CFI would issue a Solomonic ruling, upholding some of the Commission's determinations under Article 82 EC but also handing a partial victory to Microsoft. Such predictions — and other predictions of a more sweeping Microsoft victory — faced long statistical odds: it has been almost 25 years since the Commission has lost an Article 82 EC case on the substance in the courts. At least in hindsight, the allocation of the case to the CFI's Grand Chamber — only the third time it has ever been convened — might have foreshadowed that the judges deciding the case were unlikely to reach consensus on overruling the Commission or make sweeping new law in the controversial area of Article 82 EC.

Accordingly, it is not surprising that the CFI issued a very thorough and fact-oriented judgment, but one that may have limited broader significance going forward. The CFI found no manifest error in the Commission's decision. On the interoperability issue, the court observed that Microsoft had failed to substantiate its claim that an obligation to provide interoperability information would undermine its incentives to innovate, particularly given that disclosing such information is common practice in the software industry and suppliers generally believe that disclosure makes their products more attractive and valuable.

On the bundling issue, the CFI agreed with the Commission that Microsoft gained an unparalleled distribution advantage by tying WMP to its dominant Windows PC operating system. Coupled with

its decision not to make available an unbundled version of its PC operating system, Microsoft's tying decision ensured ubiquity of its media player and effectively "tipped" the balance for users and OEMs against third-party players. The CFI held that Microsoft's behavior undermined an effective competitive structure without providing any users or OEMs with any technical performance advantage.

The CFI did overrule the Commission in one respect. It held that the Commission was not authorized to delegate certain powers to the monitoring trustee. The CFI also held that the Commission had no legal basis for forcing Microsoft to pay the trustee's fees and expenses.

Implications

We offer some preliminary thoughts about the judgment's implications for several areas: development of the case-law under Article 82, impact on other pending or future cases against Microsoft and other companies, and the practical significance of the CFI's findings for the use of monitoring trustees.

Implications for the development of the law under Article 82

For the reasons explained below, the CFI's judgment makes only a modest contribution to developing the case-law applying Article 82 EC.

Interoperability. The CFI was content to pigeonhole its analysis into the Community courts' previous jurisprudence (in particular Magill and IMS Health) on the exceptional conditions under which a dominant IP-right holder may not refuse to license; that is, the refusal must (i) relate to a product or service indispensable to undertaking a particular activity in a neighboring market; (ii) exclude any effective competition in that neighboring market; and (iii) prevent the emergence of a new product for which there is potential consumer demand. The CFI did not expand on any other "exceptional circumstances" in which the refusal to license can be abusive. In particular, it declined to address the Commission's contention that some of the Magill/IMS Health criteria could be dispensed with based on other exceptional circumstances, for example the special significance that the Community legislature attaches to interoperability in the software industry, Microsoft's "super dominance" in client PC operating systems, and Microsoft having provided comparable interoperability information prior to achieving dominance in the server OS market. The CFI declined to address these proposed factors, even though it briefly referred to them later on in the judgment.

The CFI did shed some more light on the interpretation of the three parts of the Magill/IMS Health test. Although it rejected Microsoft's narrow interpretation of each part, the CFI tied its reasoning very closely to the particular facts of the case. The same was true with respect to any "objective justification" that might be available as a defense to a refusal to license claim under Article 82.

- As to the *indispensable nature* of the interoperability information at issue, the CFI first emphasized that the Commission has broad discretion to conduct this complex economic assessment, before it examined in detail the evidence on which the Commission had relied — in particular surveys of IT executives revealing that full interoperability with Microsoft's server OS was a key purchasing criterion for server operating systems.

- As to the *risk of exclusion of any competition* in the server OS market, the CFI stated that the Commission need not wait for the actual or imminent elimination of competitors before taking action, and that continuing marginal presence of competitors in certain market niches does not preclude an abuse. A contrary finding would have been surprising in light of the Community courts' precedent concerning Article 82 EC.
- The CFI's interpretation of the *new product* requirement may be more significant. The CFI relies on Article 82 (b) EC (limitation of technical development) to read the "new product" concept as extending to innovative new product features that consumers want. But in this context as well, the CFI highlights the importance of the specific factual context, namely (i) surveys showing that but for the interoperability issue, many customers believed that rivals' server OS products were better than Microsoft's; (ii) rivals having introduced innovative and popular features at a time when interoperability was not an issue; and (iii) rivals having ability and incentive to develop products that were differentiated and innovative beyond the design of interface specifications. The CFI thus does not go so far as to protect mere opportunities for product improvements absent any indication that such innovation is forthcoming or mere opportunities to produce a cheaper "me too" product. This is consistent with the ECJ's holding in *IMS Health* that the Commission could not compel licensing when the requesting company wanted to "limit itself essentially to duplicating the goods and services already offered." Indeed, a key factor in the Microsoft case was that Microsoft rivals had strong workgroup server OS offerings before Microsoft successfully leveraged its PC dominance into that market.
- *Objective justification*. The CFI gives short shrift to Microsoft's arguments that the technology in question is allegedly covered by intellectual property rights, secret, and of great value to competitors. It found that these circumstances are inherent in compulsory licensing situations and taken into account in the rule that refusals to license IPRs can be abusive only in exceptional circumstances. As to the assertion that compulsory licensing would impair Microsoft's incentives to innovate, the CFI found that Microsoft did not meet its burden to prove specifically how its incentives might be affected, particularly given that disclosure of interoperability information is common in the software industry. The CFI declined to engage in a potentially more controversial analysis of whether demonstrated disincentives to innovate for a dominant IPR holder can overcome considerations about the positive impact of a compulsory license on industry-wide innovation.

Bundling. On the specific points of the legal test under Article 82 (d) EC, the CFI's most relevant findings are as follows:

- *Separate product markets*. The CFI agreed with the Commission that, at least at the relevant point in time, Microsoft's WMP and its client PC operating system were separate products. It rejected Microsoft's view that there was no demand for its operating system without a media player as inconsistent with existing case law such as Hilti and Tetra Pak II, and instead focused on the existence of separate demand for, and supply of, streaming media players. However, the CFI recognized that as a matter of principle, especially in the fast-moving information technology sector, product convergence can occur over time so that

two products are subsequently viewed as one offering, thus escaping the tying prohibition.

- *Bundling*. The CFI confirmed that bundling the media player with the client OS amounted to tying under Article 82 (d) EC, even if consumers pay nothing extra for WMP, are not obliged to use it, and can download competitive players for free. The CFI observed that nothing in the provision's wording or the case-law suggested that any of these factors mattered.
- *Foreclosure of competition*. The CFI upheld the Commission's view that Microsoft's bundling "inevitably had significant consequences for the structure of competition," given the unparalleled distribution advantage it enjoyed as a result of its quasi-monopoly for client PC operating systems. The CFI thus held that a finding of tying did not turn on whether the two additional "stages" of the Commission's reasoning withstood scrutiny. The first of these stages was the analysis of the indirect network effects resulting from the bundled distribution, namely encouraging the development of applications and the encoding of content exclusively for WMP. The second stage was a study of the evolution of the media player market, which showed that the penetration of WMP had increased relative to that of other players. Nevertheless, seemingly taking a "belt and suspenders" approach with a view to a possible appeal, the CFI proceeded to examine the Commission's reasoning in those two additional stages and determined that it was well-founded.
- *Objective justification*. In addition to dismissing various Microsoft factual claims concerning alleged technical difficulties in offering an unbundled version, the CFI also rejected Microsoft's more fundamental proffered justification that bundling would ensure the uniform presence of media functionality in Windows, and thus relieve software developers and website creators from the burden of having to devise mechanisms to detect and, in appropriate cases, install the necessary functionality on a client PC. Although the CFI accepted that de facto "standardization" of MS' platform with its media player may promote certain efficiencies, it declined to quantify and balance those efficiencies against the anticompetitive effects of the tying at issue. Moreover, the CFI observed that nothing in the Commission's decision prevents Microsoft from releasing versions of its OS that are bundled with other software, provided that it also makes available unbundled releases.

The CFI's analysis on bundling of Microsoft's WMP with the Windows OS seems a fairly orthodox and literal application of Article 82 (d) EC. The CFI relied heavily on the provision's wording and existing case-law. In particular, it emphasized the importance of "competition on the merits." Although some may criticize the CFI for not having engaged in a more comprehensive analysis of consumer harm, it did analyze the direct elimination of consumer choice that resulted from Microsoft's bundling practice. The CFI also considered Microsoft's claimed benefits for its WMP resulting from the bundling and de-facto standardization, but observed that there was no evidence that Microsoft's media player was technically superior to those of competitors or that the bundling with Microsoft's OS resulted in a performance advantage. At bottom, the CFI's analysis is not surprising in light of the existing case law and the concern that Article 82 should proscribe purely strategic behavior that undermines competitive market structures.

Impact on other Investigations Involving Microsoft

The CFI's judgment is likely to have implications both for the pending remedies proceedings

against Microsoft and pending complaints relating to other aspects of Microsoft's behaviour.

- *Remedies proceedings*. First, the judgment is likely to have an impact on Microsoft's appeal against the Commission's 2005 decision holding that Microsoft's disclosures of interoperability information have been incomplete. Microsoft claims in this appeal that it did not understand what information it had to supply to fulfil its disclosure obligations, and that the Commission repeatedly changed its mind on this issue after it adopted the 2004 Decision. The CFI found that the Commission's 2004 Decision clearly delineated the nature and scope of the interoperability information that Microsoft had to disclose; that this information included the server-to-server protocols required for competing servers to interoperate fully with Microsoft servers; and that such required disclosures did not imply disclosure of Microsoft's internal algorithms or their specific proprietary implementations. These findings suggest that Microsoft will have difficulty convincing the CFI in its appeal that it did not understand what interoperability information it was required to disclose.

  Second, the judgment may open the door for Microsoft to claim that the annulment of certain of the monitoring trustee's oversight and enforcement powers affects the validity of the Commission's 2005 decision because that decision relied on findings by the trustee. But Microsoft seems unlikely to prevail on this point unless it can demonstrate that the Commission's decision is fundamentally grounded in findings that the trustee made using powers that the CFI has now annulled.

  Last, given that the CFI upheld all of the disclosure obligations imposed on Microsoft, the Commission is likely to press Microsoft to obtain appropriate disclosure remedies for open source software developers, as indicated in the 2005 Philip Lowe letter discussed above.

- *New complaints*. The press has reported on a number of new complaints against Microsoft since the 2004 Commission Decision. Press reports suggest that bundling complaints raised by Google, Adobe, and Symantec when Microsoft launched its new PC OS Vista were resolved through negotiations among Microsoft, the complainants, and the European Commission during fall 2006. However, the CFI's decision is likely to reinvigorate complaints concerning Microsoft's failure to disclose the information needed for competing products to interoperate with Microsoft's dominant Office Suite and Outlook/Exchange e-mail client/server software, as well as its next generation of enterprise server technology (Windows Server 2008, formerly known as Longhorn Server). The CFI's ruling confirmed that the European Commission is on sound legal footing in requiring Microsoft to disclose interoperability information when such information is essential to enable competitive product offerings to interoperate with Microsoft's market-dominating products.

Impact on other Pending Commission Art. 82 Investigations

Some have suggested that the judgment could have a substantial impact on other investigations, including those in the technology area. However, the Commission has never hinted at such a link, and it is not at all clear why it should exist. The Microsoft case combines legal and factual aspects

that are unlikely to be present in any other case. First, Microsoft holds a virtual monopoly (95% market share) for PC OS in an industry that is characterized by strong direct and indirect network effects. Second, Microsoft claimed it had IP rights for a type of information that is typically made publicly available at minimal cost, because companies recognize the added value that interoperability brings to their products. While the Commission never resolved whether Microsoft actually had IP rights that read on the interoperability specifications in question, its approach to the case may have been driven in part by the nature of this information. Third, the Commission and the CFI rejected Microsoft's standardization benefits arguments because the standards in question were imposed by Microsoft rather than the outcome of a merit-based standard setting process; the Microsoft case thus offers very limited guidance for other cases involving standards. Fourth, both the interoperability and the tying parts of the Microsoft case involved the foreclosure of rivals who were the pioneers in their respective areas and whose products were still widely viewed as superior to Microsoft's. The Microsoft case is thus not a strong precedent for situations in which would-be rivals are trying to get access to the pioneer's key technology.

Impact of the Judgment on the Use of Monitoring Trustees

As mentioned above, the CFI annulled the Commission's decision insofar as it gives the monitoring trustee powers that go beyond simply advising the Commission in performing its work. Although this is the first — and so far only — case in which the Commission has required a monitoring trustee to supervise remedies implementation in an Article 82 EC decision, the Commission has often imposed monitoring trustees in other contexts. The Commission has begun to require appointments of monitoring trustees in commitment decisions under Article 9 of Regulation 1/2003, and has consistently required them in merger cases cleared with obligations and conditions (such as divestitures). As the CFI recently confirmed in its *Alrosa* judgment, an obligation imposed in a Commission decision that merely formalizes a party's own "voluntary" commitment does not expand the Commission's powers.[5] In particular, with respect to divestiture commitments in merger cases, the Commission's practice is to require that the trustee be granted far-reaching powers, including the authority to supervise management of the business to be divested, exercise of share holder rights, appointment or removal of board members, and determining necessary ring-fencing measures. In all cases, the company giving the commitment is also required to bear the trustee's costs. The *Microsoft* judgment, however, casts doubt over the legality of the Commission's current practice. Neither Regulation 1/2003 nor the EC Merger Regulation provide for delegation of such powers to independent trustees at the parties' cost. It is also not clear whether those Regulations would provide a sufficient legal basis for the Commission itself to amend its respective implementing regulations to grant such powers to trustees. Thus, the Council may have to adopt formal amendments to Regulation 1/2003 and the Merger Regulation to create full legal certainty in this area. Of course, companies that have offered commitments involving a monitoring trustee are unlikely to challenge the trustee requirement in court. But remedy negotiations involving trustee provisions — for example, remuneration requirements — might now become less one-sided than they used to be.

[1] Case T-201/04 *Microsoft v. Commission*, Judgment of 17 September 2007, nyr, see link. WilmerHale represents interveners in support of the European Commission in the *Microsoft*

proceedings.

[2] "Assistant Attorney General for Antitrust, Thomas O. Barnett, issues statement on European Microsoft decision", Department of Justice Press Release of September 17, 2007, available here.

[3] See link.

[4] See the President's Order here, and the commentary here.

[5] See Case T-170/06, *Alrosa v. Commission*, Judgment of 11 July 2007, nyr, available at link, at paras. 88 (Commission assumes sole responsibility for commitments it declares binding) and 105-106 (voluntary nature of commitments does not relieve the Commission from observing Community legal principles such as the principle of proportionality).

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