

The JFTC renders a Recommendation to Microsoft Corporation

July 13, 2004
Fair Trade Commission

The Japan Fair Trade Commission (hereinafter "JFTC"), upon conducting an investigation into Microsoft Corporation (hereinafter "Microsoft"), found that Microsoft is conducting "Dealing on Restrictive Terms" and issued a recommendation to Microsoft on its violation of Section 19 of the Antimonopoly Act.

<p><Contact to the JFTC> First Special Investigation Division Special Investigation Department Tel: 81-3-3581-3382</p>
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1 Company Concerned

Name	Microsoft Corporation
Address	One Microsoft Way, Redmond, Washington, USA
CEO	Steve Ballmer
Primary Businesses	Software Development and Licensing, Xbox etc

2 Outlines of Violations

Microsoft, when licensing Windows OS to personal computer manufacturers (hereinafter "PC manufacturers"), has concluded agreements with PC manufacturers containing certain provisions that a licensee covenants not to sue, bring, prosecute, assist or participate in any judicial, administrative or other proceedings of any kind against Microsoft, its subsidiaries, or other licensees for infringement of the licensee's patents. Such conduct by Microsoft shall be construed as dealing with PC manufacturers on conditions which unjustly restrict their business activities, which the JFTC concluded correspond to the Subsection 13 of the Unfair Trade Practices, violating the section 19 of the Antimonopoly Act.

3 Summary of Measures to be recommended

Microsoft will terminate the certain provisions mentioned above (2) in the current and previous agreements concluded with Japanese PC manufactures.

4 Due Date of Acceptance or Rejection of this Recommendation

July 26, 2004

* If the recommendation is accepted, the JFTC will issue a decision, a legally binding order with the same elimination measures as those in this recommendation. Otherwise, the JFTC will initiate a hearing procedure.

Tentative Translation of Recommendation

1. Facts the JFTC Recognized

- (1) Microsoft drafted terms and conditions to license Windows OS, and licensed Windows OS through Microsoft Licensing General Partnership (prior to September 2003, Microsoft Licensing Inc.).
- (2) Microsoft has licensed Windows OS in an object code form, not in a source code form.
- (3) PC manufacturers can license Windows OS through 2 (two) different channels: (i) by directly negotiating terms and conditions with Microsoft (hereinafter "Direct Channel"), (ii) by purchasing compact discs with Windows OS recorded on them from distributors (hereinafter "Distributor Channel").
- (4) License agreements for Windows OS are not automatically renewed, since the duration of the license is limited to certain periods, such as 1 (one) year on or after July 2002.
- (5) Not insignificant number of PC manufacturers licensed Windows OS by Direct Channel since Distributor Channel entails rise in procuring costs and end-users suffer inconveniency in handling PCs. (Hereinafter "OEMs" refers to PC manufacturers being licensed Windows OS by Direct Channel.)
- (6) Vast majority of PCs Windows OS installed on them are manufactured by OEMs.
- (7) Since Windows 95 launched in around 1995, Windows OS has dramatically increased its market share, reaching around 95 percent in 2003. Thus, Microsoft acquires a dominant position in both world-wide market and Japanese market of PC operating system.
- (8) In 1998, Microsoft started to license Windows 98 with sophisticated audio and visual functionality applicable to digitized form of music and pictures (hereinafter "AV Functionality"), by bundling Windows Media Player. Since then, Microsoft has been expanding AV Functionality in Windows OS.
- (9) It is observed that some OEMs have been active in developing technologies of AV Functionality.
- (10) Because of its dominant position Microsoft enjoys and end-users' demands to purchase PCs with Windows OS incorporating new functionality, it is important business strategy for PC manufacturers to license the Windows OS and ship PCs at the same time when Microsoft starts to license the Windows OS.
- (11) Microsoft, since around 1993, has licensed Windows OS by concluding license agreements with OEMs which contains licensee's covenants not to sue against Microsoft, subsidiaries of Microsoft, or other licensees for infringement of the licensee's patents on account of produce or sale of Windows OS licensed to the licensees.
- (12) Around December of 2000, Microsoft presented OEMs the draft license agreement containing the following elements (hereinafter "Non-Assertion Provision") and stipulating that the following elements would survive termination or expiration of license

¹ This summary is provisional translation prepared only for reference purpose. The authentic copy is prepared only in Japanese text, which is available at the JFTC web page: <http://www2.jftc.go.jp/e-page/index.htm>.

agreement (hereinafter "Survival Provision"):

- (a) Licensee agrees not to (A) sue, or (B) bring, prosecute, assist or participate in any judicial, administrative or other proceedings of any kind against Microsoft, its subsidiaries, or other licensees for infringement of the licensees patents which occurs during the Immunity Period on account of the manufacture, use, sale, or distribution of any products licensed, or, future replacement or successor products to the products presently licensed, to the extent such future replacement or successor products embody inventions embodied in the products presently licensed,
 - (b) The licensees patents to which the above (a) applies mean all patents owned presently by the licensees, or acquired by the licensees prior to the termination or expiration of the license agreements, and
 - (c) The "Immunity Period" shall terminate upon the last to expire, of any of the licensees patents.
- (13) A part of OEMs, which owned patents in the area of technologies of AV Functionality, asserted that Non-Assertion Provision and Survival Provision would impose tremendous impact on their business. However, Microsoft did not respond to that assertion. The OEMs had no choice but to conclude the license agreement "as is".
- (14) After deciding that license agreements to be concluded on or after February 2002 should have uniform terms with regard to all OEMs, Microsoft, around December 2001, presented OEMs license agreements with licensing terms of February 2002 to July 2002.
- (15) The license agreement contained Non-Assertion Provision and Survival Provision. At this time, Non-Assertion Provision incorporated the following elements:
- (a) Licensee covenants not to (A) sue, or (B) bring, prosecute, assist or participate in any judicial, administrative or other proceedings of any kind against Microsoft, its subsidiaries, or other licensees for infringement of the licensees patents on account of the making, use, offer for sale, importation or other disposition or promotion of the products presently licensed,
 - (b) To the extent that the features and functionality presently contained in the licensed products are also contained in future replacement or successor products to the licensed products, such specific features and functionality in such future replacement or successor products shall also be considered part of the licensed products,
 - (c) The licensees patents to which the above (a) applies mean all patents owned presently by the licensees, or acquired by the licensees prior to the termination or expiration of the license agreements, and
 - (d) The covenants of (a) shall terminate as to all infringements occurring more than three (3) years after the licensee stops distributing the licensed products.
- (16) A part of OEMs, which owned patents in the area of technologies of AV Functionality, strongly requested Microsoft to delete or modify Non-Assertion Provision and Survival Provision for the following reasons:
- (a) It was likely that Windows OS infringed their patents, and
 - (b) The risk existed that they could not recoup expenditures for technology development if Microsoft continued to expand functionality of Windows OS and the OEMs' technologies would be incorporated into the coming Windows OS.

- (17) As Microsoft rejected such request, most of the OEMs had no choice but to conclude the license agreement "as is".
- (18) Thereafter, when Microsoft presented OEMs the draft license agreement with Non-Assertion Provision and Survival Provision with licensing terms of August 2002 to July 2003, and August 2003 to July 2004, A part of OEMs, which owned patents in the area of technologies of AV Functionality, strongly requested Microsoft to delete or modify Non-Assertion Provision and Survival Provision for the similar reasons mentioned (16)(a) and (b). As Microsoft rejected such request, all the OEMs had no choice but to conclude the license agreement "as is".
- (19) From the facts mentioned from (11) to (18), OEMs are precluded from suing against Microsoft or other PC manufacturers for infringement of the OEMs' patents on account of Windows OS. Especially, OEMs, which own patents in the area of technologies of AV Functionality, though they recognizes the OEMs' patents are likely to be infringed by Windows OS, are restrained to assert their patents against Microsoft or most of other PC manufacturer, and are discouraged their incentives to develop technology of AV Functionality, resulting in risks of harming fair competition in the domestic area related to the technology of AV Functionality.
- (20) Although around February 20, 2004, Microsoft represented to OEMs that it determined to delete Non-Assertion Provision prospectively from next license agreements with licensing terms between August 1, 2004; and July 31, 2005, Survival Provision in the previous agreements would continue to make Non-Assertion Provision in the previous agreements effective even after August 1, 2004.

2. Application of Law

According to the foregoing conduct, Microsoft, when licensing Windows OS, restricts PC manufactures to suing against Microsoft, its subsidiaries, or other licensees. Such conduct by Microsoft shall be construed as dealing with PC manufacturers on conditions which unjustly restrict their business activities, which the JFTC concluded correspond to the Subsection 13 of the Unfair Trade Practices, violating the section 19 of the Antimonopoly Act.

3. Elimination Measures that the JFTC Recommends

- (1) Microsoft will terminate the following terms in the current license agreements concluded with Japanese PC manufactures, which is effective until July 31, 2004.
- (a) Licensee covenants not to (A) sue, or (B) bring, prosecute, assist or participate in any judicial, administrative or other proceedings of any kind against Microsoft, its subsidiaries, or other licensees for infringement of the licensees patents on account of the making, use, offer for sale, importation or other disposition or promotion of the products presently licensed,
- (b) To the extent that the features and functionality presently contained in the licensed products are also contained in future replacement or successor products to the licensed products, such specific features and functionality in such future replacement or successor products shall also be considered part of the licensed products,

- (c) The licensees patents to which the above (a) applies mean all patents owned presently by the licensees, or acquired by the licensees prior to the termination or expiration of the license agreements, and
 - (d) The covenants of (a) shall terminate as to all infringements occurring more than three (3) years after the licensee stops distributing the licensed products.
- (2) Microsoft will terminate the following terms in the previous license agreements concluded with Japanese PC manufactures on or before July 31, 2003.
- (a) Similar term as above mentioned (1) (a) to (d),
 - (b) Licensee agrees not to (A) sue, or (B) bring, prosecute, assist or participate in any judicial, administrative or other proceedings of any kind against Microsoft, its subsidiaries, or other licensees for infringement of the licensees patents which occurs during the Immunity Period on account of the manufacture, use, sale, or distribution of any products licensed, or, future replacement or successor products to the products presently licensed, to the extent such future replacement or successor products embody inventions embodied in the products presently licensed, and
 - (c) The "Immunity Period" shall terminate upon the last to expire, of any of the licensees patents.
- (3) Microsoft will inform Japanese OEMs of the following items (a) to (c) in writing. The method of the communication shall be approved beforehand by the Commission.
- (a) Microsoft terminated certain licensing terms stated above (1) (a) to (d),
 - (b) Microsoft terminated certain licensing terms stated above (2) (a) to (c), and
 - (c) Licensees who license Windows OS will not be precluded in the future from suing, bringing, prosecuting, assisting or participating in any judicial, administrative or other proceedings of any kind against Microsoft, its subsidiaries, or other licensees for infringement of the licensees patents on account of the making, use, offer for sale, importation or other disposition or promotion of the products presently licensed Microsoft.
- (4) Microsoft, in the future and anytime when licensing Windows OS, will not preclude licensees who license Windows OS by the conclusion of any agreements or any other means whatsoever, from suing, bringing, prosecuting, assisting or participating in any judicial, administrative or other proceedings of any kind against Microsoft, its subsidiaries, or other licensees for infringement of the licensees patents on account of the making, use, offer for sale, importation or other disposition or promotion of the products licensed by Microsoft.
- (5) Microsoft will promptly report the measures adopted based on the previous four (4) items to the JFTC.