

Is it time to break Windows?

Simon Carne wonders if Microsoft should be split in two



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The United States Department of Justice believes that Microsoft has acted anti-competitively. Its court case against the software giant began four months ago.

Arguments about the issues are fraught with difficulty because the analysis so often seems to start from the wrong place. The natural tendency is to isolate specific business practices adopted by Microsoft and then consider if they are fair.

One practice, which highlights so much of the case for and against Microsoft, was to require computer manufacturers to install – and highlight in a prominent position – Microsoft's own internet browser as a condition of obtaining a licence to use its Windows operating system. This meant that software for gaining access to the internet was pre-installed in all PC-based computers.

Was this a deliberate bid to use market power to destroy other browser companies or merely the software equivalent of a motor manufacturer that decides to install its own air-conditioning system as standard?

But comparison with the motor industry – or any other industry – is unhelpful because other manufacturers are not in the same position as Microsoft. To see why, try the following experiment. Imagine a world without Microsoft.

Instead, imagine two companies. The first, OpSysCo, manufactures operating systems – the basic program, without which the computer will not work – and nothing else. The second company, AppliCo, manufactures applications programs, such as word processing, spreadsheets and internet browsers.

In all other respects, this imaginary world is the same as our world. The only real alternative to OpSysCo's operating system is the Apple Macintosh, but its system runs only on Macintosh computers. AppliCo, on the other hand, faces wide competition including, for example, Lotus in many home and office product markets, and Netscape in the internet browser market.

In this hypothetical world, OpSysCo wants software companies to write as many applications as possible to run on OpSysCo's operating system because, without applications to run, the system serves no purpose.

The more applications that run on OpSysCo's system, the greater the demand, including demand from existing users for OpSysCo to upgrade its system to provide ever-increasing speed and functionality for new applications.

And if a manufacturer of computer hardware wants to sell its machines with AppliCo applications (or Lotus applications) pre-installed, it is in

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OpSysCo's interest to encourage that, too, since computers should be as easy as possible to unpack and get started.

The same goes for AppliCo's Internet Explorer and Netscape's Navigator, the two leading Internet browsers. OpSysCo will want those packages to run on its operating system because access to the internet is one of the biggest magnets attracting new users to the computer market. This, in turn, generates more customers

for OpSysCo's system.

Now the big question. Is there any reason why OpSysCo would want to limit its product to being run with just one browser? Clearly not. Its interests are best served by encouraging more and more use of its operating system. Picking out one browser (or one word processing package) to promote at the expense of others would be good news for the chosen applications company, but it would risk other, potentially more innovative, applications manufacturers going out of business. This is not the best way for OpSysCo to ensure the continuing expansion of its own market.

Realistically, the only way in which OpSysCo has an incentive to authorise only one applications manufacturer in any product area is if the chosen applications company rewards OpSysCo, in cash or by some other means, for its refusal to licence any competing application programs from running on its operating system.

Such an agreement would deny the other applications manufacturers access to 90 per cent of the market, which is obviously anti-competitive. The deal would, rightly, be struck down by the competition authorities.

For the same reason, any proposal to merge OpSysCo with AppliCo would certainly be rejected by the competition authorities, precisely because such a merger would have no commercial rationale other than the opportunity it presented for anti-competitive collaboration.

Back in the real world, Microsoft's operating and applications businesses have always been part of one company and, until recently, its operating system business appeared to be happy doing business with all applications manufacturers, including those who competed with Microsoft's own applications.

If Microsoft now wishes its operating systems business to enforce exclusive deals for the benefit of its own applications system business, the competition authorities should ask themselves two simple questions. Would such a deal be lawful in a hypothetical world in which the two businesses were separate? Would a merger be allowed between two companies who proposed to operate such a deal?

If the answer to either question is "no" in the hypothetical world, the answer should be "no" in the real world, too.