Microsoft to pay $750m to settle AOL antitrust case

Former foes agree to truce, collaboration

By Hiawatha Bray, Globe Staff, 5/30/2003

The Internet browser war that began on Pearl Harbor Day of 1995 ended yesterday, as Microsoft Corp. reached a $750 million settlement of an antitrust case filed by AOL Time Warner Inc.

Top executives of the two technology giants said the settlement marked a truce - and a new collaboration. "It puts any past issues behind us," said Microsoft chairman Bill Gates. "It's a forward-looking agreement."

AOL chairman Dick Parsons struck an equally conciliatory tone. "We welcome the opportunity to build a more productive relationship with Microsoft going forward," he said.

Indeed, the bad blood between Microsoft and AOL Time Warner seems to have been washed away by a shared concern about the public's burgeoning demand for digital entertainment. Instead of squabbling over browser market share, the two companies said they will work on new digital media technologies that will combine ease of use with tough defenses against illegal copying of digital music and video files.

The deal settles a private antitrust suit filed in January 2002. The case grew out of Microsoft's aggressive campaign to dominate the market for Internet browsing software. In 1995, that new market was dominated by software from Netscape Communications Corp., which was later acquired by AOL Time Warner. On Dec. 7, 1995, Gates sent a memo to Microsoft employees, committing them to a relentless counterattack against the surprise success of Netscape.

Microsoft's efforts to persuade computer companies to adopt its Internet Explorer browser, which it bundled for free in its Windows operating system, earned Microsoft near-total dominance in Internet browsers.

It also brought Microsoft to the brink of court-ordered dissolution, after the company's tactics inspired one of the biggest antitrust cases in US history, a case that Microsoft lost. The judgment that proposed a breakup...
of Microsoft was later set aside in favor of milder penalties.

But a variety of state governments and private businesses filed separate suits against Microsoft, basing their complaints on the successful antitrust case. AOL Time Warner's Netscape business unit sought not only damages from Microsoft, but also injunctions that could have forced Microsoft to distribute copies of Netscape's browsing software along with its own in future versions of Microsoft's Windows operating system.

Now those demands have been abandoned and the case is closed, thanks in part to a badly needed cash infusion for AOL.

"We're going to use the settlement proceeds just to retire some debt," said Parsons, who estimated that his company is about $24 billion in debt.

Roger Kay, analyst for the technology research firm IDC, thinks this financial motivation was a key reason for the settlement. "AOL has a problem with its debt, and Microsoft has a pile of cash," Kay said. "That makes good sense from a business perspective."

Another spur to a settlement could be the need for both companies to embrace digital media technologies. In a key portion of the agreement, AOL agreed to long-term licensing of Microsoft's Windows Media software for video and audio services. The companies said they will also work together on "digital rights management" systems that will allow consumers to download and use files, but will set limits on their ability to copy and share them with others who haven't paid for them.

AOL and Microsoft agreed not only to work on technologies to address the issue, but even to present a united front in lobbying elected officials for laws to protect the copyrights of digital media producers.

Indeed, Kay said that the success of Apple Computer Inc.'s iTunes Music Store, which has sold millions of songs over the Internet, may have given the companies an extra nudge toward doing a deal.

"I think that might have been a stimulus," Kay said, partly because iTunes uses its own digital media format that competes directly against Microsoft's.

A pact with AOL would allow the two partners to create a music service aimed at the 35 million worldwide subscribers to the America Online Internet service. And the AOL-Microsoft service could offer music encoded in the Microsoft format.

"Clearly it's a big boost in the arm for Microsoft's efforts in this area," said David Smith, Microsoft analyst for Gartner Inc.

In another significant move, the two companies agreed to work together on making their instant messaging programs compatible. AOL has long
resisted letting Microsoft or anyone else connect to its instant messaging system, by far the world's most popular with about 150 million users. But Gates and Parsons wouldn't say when the goal of compatibility would be achieved.

As for the Netscape browser, the agreement puts its future in doubt. AOL doesn't even use it, having chosen Microsoft's instead.

"Frankly, it's worked very well," Parsons said. And with the new deal, AOL will continue to use Microsoft's browser in its software for the next seven years under a royalty-free contract.

Parsons said there were a variety of "possibilities" for Netscape and its roughly 300 employees, but he declined to reveal them.

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