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Message 47:  
From billp Mon Apr 23 22:37:45 1990  
To: billg johnsa mikehal steveb tonya  
Subject: DLA - different royalty structure  
Cc: billp  
Date: Mon Apr 23 22:37:34 1990

For the sake of argument I'd like to propose a different structure which has the following points:

1. IBM identifies which product is its "OEM Product" and which product is its "Retail Product". IBM will use reasonable efforts to make sure that IBM OEM Product gets sold only to an end user who contemporaneously (more or less) purchases a "Covered System" or as an upgrade for a "Covered System". IBM Retail Product can be sold without such restriction.
2. Essentially same definitions for MS "OEM Product" (though it is tied to our OEMs' machines) and MS "Retail Product" (all MS packaged product except packages sold to OEMs to bundle only with systems).
3. IBM pays us \$X per system for IBM Covered Systems to cover IBM OEM Product. MS pays IBM nothing for MS OEM Product.
4. Determine for each applicable period (beforehand, if possible) what percentage of all X-86 machines shipping are IBM Covered Systems ("Y %"). Therefore, the rest of the market is 1-Y%.
5. If 100 is the number of IBM Retail Product/DOS that IBM ships in the applicable quarter, then we assume that  $(100)(1-Y\%)$  is the number that got onto non-Covered Systems. Whatever that number works out to be, IBM pays MS some per copy royalty for each. This royalty is different for each Retail Product.
6. Same math for MS, except the assumption is that  $(100)(Y\%)$  is the number that got sold onto Covered Systems. We pay the per copy royalty to IBM for those copies.
7. The per copy royalty that IBM pays and that MS pays should not eat up all the profit on that copy. Otherwise it is more profitable for IBM to sit back and allow us to pay them more than our profit (which is certainly more than IBM's profit) for each copy sold onto IBM machines. I don't know the profit

structure for our products, but 12.5% of SRP for our retail products sounds like it could provide that kind of disincentive to IBM and is punitive to MS. How about something based on net revenues rather than SRP, which is a rather artificial number in any case? 5% of net revenues, say.

The data available to determine what percentage of the X-86 market is Covered Systems is probably more reliable and cheaper to get than the information required in the current audit proposal. The major difficulty is that it requires some adjustment in the way that IBM does business currently, but other OEMs manage it. The disadvantage to MS is that for some period of time the percentage of IBM Retail Product that actually gets sold for use on non-Covered Systems is

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higher than the percentage we use to determine which ones IBM pays  
as a royalty on (i.e. the number of non-Covered Systems shipping  
now as a percentage of all x-86 systems shipping now). However, given  
the way IBM distributes product it may not be much higher and over time  
it will probably drop below that percentage.

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New mail has arrived -- type 'restart' to read.

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Message 48:

From billp Tue Apr 24 09:06:30 1990

To: billg johnsa mikehal steveb tonya

Subject: DLA - different sroyalty structure

Cc: billp

Date: Tue Apr 24 09:06:25 1990

Privilege Material  
Redacted

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>From billg Tue Apr 24 00:09:25 1990  
To: billp johnsa mikehal steveb tonya  
Subject: DLA - different sroyalty structure  
Date: Tue Apr 24 00:06:59 1990

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Redacted

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Message 43:

From jons Mon Apr 23 12:25:26 1990

To: billg billn frankga jeremybu joachimk jonl mikehal paulma russw  
C billp johnsa steveb tonya

Subject: RE: IBM discussions

Date: Mon Apr 23 12:24:15 1990

This is a very interesting plan but I do not see how the cross royalty could work. The situation today is that there is huge IBM leakage onto other systems. Many corporations buy only IBM DOS. There is very little leakage the other way except through piracy of various kinds.

It would seem to me that there is no way to measure leakage. Who is to know what hardware a copy of IBM DOS sold by Egghead will end up on? Or for that matter if Businessland sells NCR machines with Compaq DOS. I guess you could do instore surveys world wide but who would believe them?

Windows leakage would depend on how IBM supports it. If they bundle it with DOS 100% then they would be the leakers. if they just sell it and we continue on our retail strategy then ?

we would out leak them a lot.

The DOS RUP becomes impossible unless there is a special plan for upgrades. The flow to them would be high.

The only sure way would be for both sides to either make the products not run on the others turf or to carry two versions, the will run on IBM hardware and the will not run on IBM hardware. That would be interesting for the channel to figure out.

Assuming the latter was done then the royalty should not be based on SRP but net revenues. What is the SRP of Microsft OEM only DOS? If it is the same as the IBM DOS then we would lost money on almost all OEM leakage.

It would help if I understood their (or our) rationale for this kind of deal. Do they think we sell a lot on their systems? Do they want to sell a lot on other OEM systems? If the issue is only IBM doing direct selling to OEMs that would trigger the royalty I guess I could understand that but they would still have all the retail leakage.

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The basic problem with DOS is that we sell OEM and they sell retail. When we get to products that we both sell retail then the only option is to sell IBM specific work or not work product.

I assume the royalty for OS products that they pay goes across all products, including DOS?

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