

*Judy -
FYI - Janet*

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Dear Judy and Liz,

Since the beginning of 1988 we have discussed the exciting Windows and Mouse opportunity that exist for Compaq. During numerous meetings and presentations we have addressed the essential issues that have been raised. To clarify today's situation I want to summarize the key issues and proposals.

Basic Business Proposal regarding Windows and Mouse:

The proposal discussed is that Compaq bundles Windows with DOS when Microsoft ships and announces Windows 3.0 late summer 88. This package would be sold as an 'Ease-Of-Use/Power' retail package to be available by all Compaq authorized dealers. The setup would be merging Windows and DOS in a fashion making it very easy to install. Simultaneously Compaq would commence shipping a Microsoft Mouse with a Compaq logo with every system that goes out.

Response to Compaq's main requirements for making a commitment:

Based on my experience working with Compaq there are four key elements that need to be satisfied in order for Compaq to make a commitment. The product should fit into Compaq's long term strategy, the product should add unique value to the Compaq offering without infringing on the dealer's business, the product should display Compaq high performance hardware preferably relating to the 386 line and finally it must make financial sense. Below I am addressing these elements together with specific offers Microsoft has given to Compaq over the last year.

The Product should fit with Compaq's long term strategy:

Compaq is developing an ease-of-use story that counteracts Apple's success in the large account market. Further, Compaq needs to establish a leadership position in terms of Ease-Of-Use within the EISA group. The DOS/Windows packaging together with the system Mouse provide these benefits.

The Product must add unique value to the Compaq offering (without infringing on the dealer's business):

What I see as important here is that Compaq either has better performance than the competition or has time to market advantage. By working with Microsoft early Compaq would be positioned to ship the unique Windows 3 product at the same time Microsoft announces the product. I suggest Compaq becomes the key partner for testing and usability studies as well as work on the BAK. This cooperation would by default lead to time to market advantage.

To have the Mouse ship with every system will add leadership to Compaq's ease-of-use story while making it easier for your dealers to set up and install your systems in a fashion that puts Compaq ahead of the competition.

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The Product must display Compaq high performance hardware

Windows 3 will in a unique way display the performance and features of Compaq's recent monitor and graphics board(L0140768) as well as the to be released TIGA product. Naturally Compaq's high performance systems would take advantage of Windows 3 since the product is being developed on Compaq systems.

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Plaintiff's Exhibit
5030
Comes V. Microsoft

EXH. 2 DATE 4/1/88
WITNESS Susan Zielie
SUSAN ZIELIE

**DEFENDANT'S
EXHIBIT
4026**

The decision must make financial sense:

Below is Microsoft's aggressive royalty quote (per system) that is valid through March 15th.

Processor:	Windows 3 + Shell	Quote Comdex	Final royalty quote	Negotiated
8086/80	\$12+\$1=\$13	\$10+\$0=\$10	(3)	
80286	\$12+\$1=\$13	\$12+\$0=\$12	(1)	
80386	\$15+\$1=\$16	\$14+\$0=\$14	(2)	

The margin you could gain with a DOS/Windows package is significant as the SRP for DOS is \$150 and Windows SRP is \$80 and \$105 currently (to be raised with Windows 3). Assuming COGS of \$25 and a Compaq SRP of \$250 the gross margin retained by Compaq would be approximately 58% i.e. well above Compaq's average 40% gross margin.

The following are prices for the OEM version of the Microsoft Mouse:

50,000 unit annual commitment @ \$22.00 per copy when shipped with a customer system
100,000 unit annual commitment @ \$20.00 per copy when shipped with a customer system

To further make the offer financially attractive we would consider the following ideas:

Compaq could purchase Microsoft's finished goods manuals
Compaq could apply the Windows and Mouse payments towards the OS/2 minimum commitments
Up-grade of Compaq's Win/386 inventory to 2.11 free of charge through master disks.

Unique offers given by Microsoft for this particular opportunity:

- 90 day support for Windows from date of shipment provided by the PSS division at no charge
- Six month labeling promotion of the "PS/2" Mouse with Compaq
- Marketing support for the announcement
- Up-grade of the current inventory in Houston
- Microsoft Sales PAD for Compaq field people providing them with needed sales tools at a cost basis (incl Win386, Mouse, Excel plus demo, training and reference materials)
- Early code to Compaq for testing and usability work
- Designated Windows contact points at the local MS offices
- Strong Microsoft presence at the announcement

Request for commitment:

We are getting very close to the date when I no longer can keep the above options open on your behalf. The Windows 3 project is proceeding rapidly as are ideas around the DOS/Windows concept. In order for Microsoft to adhere to the above I need your final decision by March 15th. Work in this area could then proceed based on a signed LOI between our Companies.

I look forward to discussing the above with you in person next week.

Best Regards

Jan Claesson

Group Manager
OEM Division

cc: Mike Clark Richard Fade
 Gary Stines Rich Abel
 Tom Parish

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