

A Perverse Use of Antitrust Law.

by Charles T. Munger. September 2000.

As best I can judge from the Microsoft antitrust case, the Justice Department believes that any seller of an ever-evolving, many-featured product--a product that is constantly being improved by adding new features to every new model--will automatically violate antitrust law if: (1) it regularly sells its product at one all-features-included price; (2) it has a dominant market share and (3) the seller plays "catch-up" by adding an obviously essential feature that has the same function as a product first marketed by someone else.

If appellate courts are foolish enough to go along with the trial court ruling in the Microsoft case, virtually every dominant high-tech business in the United States will be forced to retreat from what is standard competitive practice for firms all over the world when they are threatened by better technology first marketed elsewhere.

No other country so ties the hands of its strongest businesses. We can see why by taking a look at America's own history. Consider the Ford Motor Co. When it was the dominant U.S. automaker in 1912, a small firm--a predecessor of General Motors--invented a self-starter that the driver could use from inside the car instead of getting out to crank the engine. What Ford did in response was to add a self-starter of its own to its cars (its "one-price" package)--thus bolstering its dominant business and limiting the inroads of its small competitor. Do we really want that kind of conduct to be illegal?

Or consider Boeing. Assume Boeing is selling 90 percent of U.S. airliners, always on a one-price basis despite the continuous addition of better features to the planes. Do we really want Boeing to stop trying to make its competitive position stronger--as it also helps travelers and improves safety by adding these desirable features--just because some of these features were first marketed by other manufacturers?

The questions posed by the Microsoft case are: (1) what constitutes the impermissible and illegal practice of "tying" a separate new product to a dominant old product, and (2) what constitutes the permissible and legal practice of improving an existing one-price product that is dominant in the market.

The solution, to avoid ridiculous results and arguments, is easy. We need a

simple, improvement-friendly rule that a new feature is always a permissible improvement if there is any plausible argument whatever that product users are in some way better off.

It is the nature of the modern era that the highest standards of living usually come where we find many super-successful corporations that keep their high market shares mostly through fanatical devotion to improving one-price products.

In recent years, one microeconomic trend has been crucial in helping the United States play catch-up against foreign manufacturers that had developed better and cheaper products: our manufacturers learned to buy ever-larger, one-price packages of features from fewer and more-trusted suppliers. This essential modern trend is now threatened by the Justice Department.

Microsoft may have some peculiarities of culture that many people don't like, but it could well be that good software is now best developed within such a culture. Microsoft may have been unwise to deny that it paid attention to the competitive effects of its actions. But this is the course legal advisers often recommend in a case such as this one, where individuals' motives at Microsoft were mixed and differed from person to person. A proper antitrust policy should not materially penalize defendants who make the government prove its case. The incumbent rulers of the Justice Department are not fit to hold in trust the guidance of antitrust policy if they allow such considerations of litigation style to govern the development of antitrust law, a serious business with serious consequences outside the case in question.

While I have never owned a share of Microsoft, I have long watched the improvement of its software from two vantage points. First, I am an officer and part owner of Berkshire Hathaway Inc., publisher of the World Book Encyclopedia, a product I much admire because I know how hard it was to create and because I grew up with it and found that it helped me throughout a long life.

But despite our careful stewardship of World Book, the value of its encyclopedia business was grossly and permanently impaired when Microsoft started including a whole encyclopedia, at virtually no addition in price, in its software package. Moreover, I believe Microsoft did this hoping to improve its strong business and knowing it would hurt ours.

Even so, and despite the huge damage to World Book, I believe Microsoft was entitled to improve its software as it did, and that our society gains

greatly--despite some damage to some companies--when its strong businesses are able to improve their products enough to stay strong. Second, I am chairman and part owner of Daily Journal Corp., publisher of many small newspapers much read by lawyers and judges. Long ago, this corporation was in thrall to IBM for its highly computerized operation. Then it was in thrall to DEC for an even more computerized operation. Now it uses, on a virtually 100 percent basis, amazingly cheap Microsoft software in personal computers, in a still more highly computerized operation including Internet access that makes use of Microsoft's browsers.

Given this history of vanished once-dominant suppliers to Daily Journal Corp., Microsoft's business position looks precarious to me. Yet, for a while at least, the pervasiveness of Microsoft products in our business and elsewhere helps us--as well as the courts that make use of our publications--in a huge way.

But Microsoft software would be a lousy product for us and the courts if the company were not always improving it by adding features such as Explorer, the Internet browser Microsoft was forced to add to Windows on a catch-up basis if it didn't want to start moving backward instead of forward.

The Justice Department could hardly have come up with a more harmful set of demands than those it now makes. If it wins, our country will end up hobbling its best-performing high-tech businesses. And this will be done in an attempt to get public benefits that no one can rationally predict.

Andy Grove of Intel, a company that not long ago was forced out of a silicon chip business in which it was once dominant, has been widely quoted as describing his business as one in which "only the paranoid survive." If this is so, as seems likely, then Microsoft should get a medal, not an antitrust prosecution, for being so fearful of being left behind and so passionate about improving its products.

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