UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

UNITED STATES OF AMERICA,	)	
Plaintiff,	)	
v.	)	Civil Action No. 72-344 (AGS)
INTERNATIONAL BUSINESS MACHINES CORPORATION,	)	
Defendant.	)	

UNITED STATES' MEMORANDUM IN SUPPORT OF ITS MOTION TO COMPEL DISCOVERY

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UNITED STATES' MEMORANDUM IN SUPPORT OF ITS MOTION TO COMPEL DISCOVERY

Pursuant to Rule 37(a) of the Federal Rules of Civil Procedure, the United States of America (the "Government") respectfully submits this Memorandum in support of its motion to compel International Business Machines Corporation ("IBM") to produce information and documents responsive to the Government's August 4, 1995, Interrogatories and Requests for Production of Documents.[1]

I. Background

This proceeding commenced on June 13, 1994, when IBM filed a motion to terminate the Final Judgment ("decree") in this action. IBM also moved to disqualify the presiding judge, David N. Edelstein, so the motion for termination was held in abeyance pending resolution of the disqualification motion. Judge Edelstein denied the disqualification motion on July 28, 1994, and IBM petitioned the Court of Appeals for a writ of mandamus. On January 17, 1995, the Court of Appeals issued a writ of mandamus directing Judge Edelstein to recuse himself, and on February 2, 1995, the case was reassigned to Judge Schwartz.

At a March 1, 1995 hearing, the Court asked the parties to submit memoranda setting forth the issues raised by IBM's motion.

Appended as tab 6 to the Declaration of James J. Tierney, May 24, 1996, (Tierney decl."); all other tabbed materials cited herein are likewise appended thereto. Copies of the cases cited herein are also provided to the Court under separate cover and arranged alphabetically.

IBM filed its *Preliminary Statement of Issues* ("*IBM Prelim.*") on June 6, 1995 (tab 2) and the Government filed its *Preliminary Statement of Issues* ("*U.S. Prelim.*") on July 19, 1995 (tab 4). In its filing, the Government expressed its tentative decision to join IBM's motion as to certain decree provisions and certain IBM products. (*Id.* at 2.) For the remaining decree provisions and the remaining products -- IBM's S/360. . . 390 mainframe and AS/400 mid-range families of computer products and services -- the Government requested and was permitted a period in which to investigate the issues raised by IBM's motion in order to determine whether to join or oppose IBM's motion.

On April 19, 1996, the Government advised the Court that we would agree, after an appropriate sunset period, to terminate the decree as it applies to the AS/400 products and services. On June 28, 1996, the Government will advise the Court on its view as to an appropriate sunset period for the AS/400 and it will inform the Court of its position on the merits of decree termination as it applies to IBM's S/360. . . 390 family of products and services. Absent resolution of the remaining AS/400 and S/360. . . 390 issues by consent of the parties, a hearing on IBM's motion to terminate the decree is to commence on March 24, 1997. (*See Proposed Scheduling Order* (dated May 1, 1996), tab 7; *Stipulation and Order* (dated May 22, 1996), tab 5.)

On August 4, 1995, in furtherance of our investigation as to

the AS/400 and S/360. . . 390 products and services, the Government served upon IBM Interrogatories and Requests for the Production of Documents. IBM initially refused to respond to the Government's requests, but on January 16, 1996, it agreed to produce some readily responsive information and some high level planning documents located at IBM's headquarters. (*See Tierney decl., ¶8.)* The Government accepted IBM's partial responses but expressly reserved the right to seek more complete responses as necessary to complete our investigation, and absent a consensual resolution of this matter, to prepare for litigation of IBM's motion. (*Id.* ¶¶30, 32.) Pursuant to the Court's Scheduling Order of May 1, 1996, motions to compel discovery must be filed by May 24, 1996.

To date, IBM has only partially complied with a number of requests and it has continued to refuse to comply with several others. Asserting lack of relevance, IBM has broadly objected to requests for information and documents it construes to be "related to the presence or absence of monopoly or market power in any 'markets' or 'sub-markets' for electronic data processing machines." (*IBM Objections to Plaintiff's Interrogatories and Document Requests* ("*IBM May 10, 1996 Objections*") (dated May 10, 1996), tab 13, ¶5.) IBM also refuses, on grounds of relevance, to comply with discovery requests that seek information relating to operating system software, information relating to IBM

disclosures of interface information, and information from IBM's operations outside the United States. (*Tierney decl.*, ¶12.) In addition, the Government and IBM have not been able to agree upon a mechanism to preserve the Government's right to seek additional responses to outstanding requests beyond the May 24 deadline for motions to compel set forth in the May 1, 1996 Scheduling Order. (*Id.*)

IBM's refusal to produce the requested information and documents will seriously undermine the Court's ability to make an informed decision on the merits of IBM's motion. IBM's refusal to comply with what it deems to be "market-related" discovery is based on the erroneous proposition that a market analysis is not necessary to the Court's disposition of IBM's motion to terminate the decree. (*Id.* ¶18.) As we previously have explained and will reiterate in this memorandum, IBM's position is contrary to governing law that requires the assessment of market power in properly defined markets as a general predicate to the disposition of a motion to terminate an antitrust decree. IBM's other relevance objections with respect to discovery relating to operating system software, IBM's disclosure of interface information, and information from its foreign locations are equally misplaced, as we discuss below. Finally, we explain why IBM should be ordered to produce certain information and documents that up until now the Government has permitted IBM to

defer from its responses.

In addition to the unsustainable relevance objections, IBM objects to the Government's discovery requests due to generalized claims of vagueness, ambiguity, overbreadth, and burdensomeness. The Government has had several discussions with IBM in an effort to address comprehensively IBM's objections in order to forestall this motion to compel. IBM has expressed a preference to resolve the issues of relevance in the first instance, and to the extent these issues are resolved in favor of discovery, the parties will attempt to work out any remaining questions as to burden before seeking any further consideration by the Court. (*Id.* ¶13.) The Government does not object to this approach.

II. The General Standard Of Relevance

Before we show why IBM's relevance objections are unfounded, we briefly review the standard of relevance under the Federal Rules of Civil Procedure. In pertinent part, Fed. R. Civ. P. 26(b)(1) states that "[p]arties may obtain discovery regarding any matter, not privileged, which is relevant to the subject matter involved in the pending action . . . ." Information is relevant so long as it is reasonably calculated to lead to the discovery of admissible evidence. *See Daval Steel Products v. M/V Fakredine, 951 F.2d 1357, 1367 (2d Cir. 1991). It is not grounds for an objection that the information sought will be inadmissible at trial so long as the requested material could*

lead to other information that may be relevant to the subject matter of the action and "[t]his obviously broad rule is liberally construed." Id. (citing Oppenheimer Fund, Inc. v. Sanders, 437 U.S. 340, 351 (1978) (relevance under rule 26(b)(1) is broadly construed "to encompass any matter that bears on, or that reasonably could lead to other matter that could bear on, any issue that is or may be in the case") (emphasis added). Accord Maresco v. Evans Chemetics, Div. 964 F.2d 106, 114 (2d Cir. 1992) ("the scope of discovery under Fed. R. Civ. P. 26(b) is very broad"); Paper Corp. of the United States v. Schoeller Tech. Papers, 759 F. Supp. 1039, 1048 (S.D.N.Y. 1991) ("the phrase 'relevant to any subject matter involved in the pending action' has been construed broadly to 'encompass any matter that bears on, or that reasonably could lead to other matter that could bear on, any issue that is or may be in the case'") (quoting Hickman v. Taylor, 329 U.S. 495, 501 (1947)); Morse/Diesel, Inc. v. Fidelity & Deposit Co., 122 F.R.D. 447, 449 (S.D.N.Y. 1988) (term "reasonably calculated" means "any possibility that the information sought may be relevant to the subject matter of the action.").

As we discuss below, the issues towards which the Government's discovery is directed are at the core of this proceeding.

III. IBM Should Be Ordered To Produce Information And Documents Relevant To Market Analysis And Other Equitable Considerations Essential To Disposition Of IBM's Motion To Terminate The Decree

The Government's discovery is aimed at obtaining evidence about IBM's ability to exercise market power, which is, consistent with Fed. R. Civ. P. 26(b)(1), a "matter . . . relevant to the subject matter" at issue. A market analysis is necessary to determine whether termination would further the public interest in competition, or to the contrary, whether it would undermine the public interest by freeing IBM from the decree's constraints on its ability to exercise market power in properly defined markets. The same evidence is relevant to determine whether eliminating the decree is equitable to consumers and other entities that have relied on the marketplace conditions and practices that the decree long ago established. IBM disputes the Government's position as to whether a market power inquiry is necessitated by IBM's motion. The parties already have extensively briefed the issue and the matter is before the Court.[2]

Pending the Court's decision on the need for market analysis, IBM generally has refused to comply with the

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See United States' Memorandum on the 1969 Case ("U.S. 1969 Mem.") (dated October 5, 1995), tab 16, at 1-2; 9-19; 21 n.14; *U.S. Prelim.*, tab 4, at 1; 17-21; 24-45; IBM Prelim., tab 2; *IBM's Memorandum Addressing the Significance of the Government's 1969 Case* (dated September 7, 1995).

Government's discovery requests as to "market-related" evidence:

> *on the grounds that they are not reasonably calculated to lead to the discovery of admissible evidence <u>to the extent that they seek information purportedly related to the presence or absence of monopoly or market power in any "markets" or "sub-markets" for electronic data processing machines</u>.*

(IBM May 10, 1996 Objections, tab 11, ¶5, (emphasis added).) It is important to understand that IBM's objection is not founded on a claim that the Government's discovery is not relevant to market analysis. Rather, the objection is based on the erroneous argument that the decree has nothing to do with market power, hence a market analysis has no bearing on the Court's consideration of IBM's motion. Indeed, IBM can not plausibly claim that the Government's requests are not relevant to market power issues, for it has all but conceded such relevance. (See 10/30/95 Tr., tab 18, at 82 ("[v]irtually all of [the Government's discovery request], your Honor, . . . goes on the question of whether we [IBM] have a monopoly in a number of computer markets or not."); Tierney decl., ¶18.)

Although the Court has not yet resolved the fundamental difference between the Government and IBM with respect to the role of market analysis in this proceeding, even in the absence of such resolution, the information and documents requested from IBM are relevant to the equitable issues that the Court ultimately must address, notwithstanding IBM's protestations

about the relevance of market power discovery.

A. Whether IBM Possesses Market Power In Properly Defined Markets Is Relevant To The Disposition Of IBM's Motion And Thus Discoverable

On May 1, 1996, notwithstanding the pendency of the issues pertaining to market analysis, the Court entered a scheduling order that contemplates that the parties would proceed with previously served discovery requests. In so doing, the Court did not accommodate IBM's view that IBM should be allowed to hold in abeyance the Government's requests as to "market issues" until the Court rules on the need to conduct a market power analysis. (See 08/07/95 Tr., tab 17, at 44-46; 10/30/95 Tr., tab 18, at 95).

The Government's market power discovery should go forward because the law requires that a market power analysis be performed. Indeed, the Court of Appeals for the Second Circuit recently has spoken on the issue in United States v. Eastman Kodak Co., 63 F.3d 95 (2d Cir. 1995). There, the Court of Appeals affirmed the District Court's market power inquiry in the termination of two antitrust consent decrees entered in 1921 and 1954 that enjoined the defendant from a variety of potentially anticompetitive practices with respect to photographic film and photofinishing products and services. Just as the Government has urged the Court in this case, in Kodak the District Court employed standard antitrust analysis -- including the definition

of relevant product and geographic markets and the evaluation of other issues relating to market structure -- to determine whether Kodak possessed market power in properly defined markets. With respect to the 1921 Kodak decree, the Court's reliance on standard antitrust analysis led it to consider the likely market effects of termination with specific reference to the relevant market for color photographic film. The Court arrived at this definition of the relevant product market even though the decree had been predicated on defendant's monopolization of an overarching "market" for photographic supplies, which covered all kinds of related products, such as cameras, film, plates, and photographic paper. United States v. Eastman Kodak Co., 853 F. Supp. 1454, 1467, 1483-85 (W.D.N.Y. 1994); see also U.S. 1969 Mem., tab 16, at 17-18.

In affirming the District Court in Kodak, the Court of Appeals recognized that equitable considerations must guide a court's analysis as to whether to vacate an antitrust consent decree. Kodak, 63 F.3d at 101 (citing Rufo v. Inmates of Suffolk County Jail, 502 U.S. 367 (1992)). The Court of Appeals also reiterated that the standard set forth in United States v. United Shoe Mach. Corp., 391 U.S. 244 (1968) is the burden that antitrust defendants should be expected to satisfy in seeking termination of an antitrust decree:

However, we also believe that United Shoe provides a

> *useful starting point for evaluating an antitrust defendant's request to modify or terminate a consent decree. In most cases, the antitrust defendant should be prepared to demonstrate that the basic purposes of the consent decrees -- the elimination of monopoly and unduly restrictive practices -- have been achieved.*

Kodak, 63 F.3d at 101 (citing United Shoe, 391 U.S. at 248) (emphasis added). Though acknowledging that other limited circumstances may justify modification or termination of an antitrust consent decree (for instance when controlling law has changed or when the decree is ineffective in accomplishing its goals), the Court of Appeals stated that:

> *[A]s a general matter, . . . an antitrust defendant should not be relieved of the restrictions that it voluntarily accepted until the purpose of the decree has been substantially effectuated, or when time and experience demonstrate that the decree is not properly adapted to accomplishing its purposes.*

Kodak, 63 F.3d at 102 (citation & internal quotation marks omitted). A market analysis is required to determine whether the purpose of an antitrust decree has been fully achieved or if changed circumstances have rendered the decree incapable of accomplishing its purposes and in Kodak the court undertook that analysis:

> *In determining whether a firm possesses market power, "the first step in a court's analysis must be a definition of the relevant markets." Berkey Photo, Inc. v. Eastman Kodak Co., 603 F.2d 263, 268 (2d Cir. 1979), cert. denied, 444 U.S. 1093 (1980). Without a definition of the relevant market, there is no way to measure a company's ability to act as a monopolist. Walker Process Equip., Inc. v. Food Mach. & Chem. Corp., 382 U.S. 172, 177 (1965).*

Kodak, 63 F.3d at 104. The Court of Appeals concluded that the District Court had applied the correct legal principles and that its factual findings were not clearly erroneous. Id. at 109.

A market analysis is necessary because it will permit an assessment of the likely effects of decree termination. Here, the Court clearly recognized the relevance of the likely effects of decree termination when it allowed Government discovery to proceed unilaterally as to IBM's post-termination plans. However, IBM's future conduct in the event of termination will depend on how termination will effect IBM's ability to avoid or undermine competition that currently is facilitated by the decree. The case law makes clear that this assessment of the likely effects of termination can only be meaningful in the context of standard antitrust analysis.

Just as market power issues were at the core of the Kodak proceeding, so too, they are central to this resolution of the instant motion. In light of this controlling case law, the Government's discovery falls squarely within the scope of Fed. R. Civ. P. 26(b)(1). Indeed, analysis under Fed. R. Civ. P. 26(b)(1) focuses on the likelihood of whether the requested information has a possible bearing upon the subject matter at issue. We have amply satisfied this standard. See, e.g., Jones v. Boeing, Co., 163 F.R.D. 15, 16 (D. Kan. 1995) ("[a] request for discovery should be considered relevant if there is any

possibility that the information sought may be relevant to the subject matter of this action. Discovery should ordinarily be allowed under the concept of relevancy unless it is clear that the information sought can have no possible bearing upon the subject matter of this action.") (citations omitted & emphasis added).

Although Kodak teaches that a defendant ordinarily should not be relieved of a consent decree if elimination of monopoly power and restrictive practices has not occurred, IBM disputes the import of that case, resting its argument that a market power analysis is unwarranted on the incorrect supposition that the purpose of its decree in applying to computers was strictly to prevent it from leveraging its tabulating machine monopoly power in to computers -- an argument that we have refuted and is now before the Court. (U.S. 1969 Mem., tab 16, at 11-14.) But IBM also is unwilling to stipulate that it possesses market power for the purposes of this proceeding (10/30/95 Tr., tab 18, at 77-79) and it raises its purported lack of market power in countering the Government's concerns, thereby effectively placing market power in issue. (See Memorandum of Law in Support of IBM's Motion to Terminate the 1956 Consent Decree (dated August 24, 1993), tab 21, at 10 ("However any likely relevant market is defined, IBM's share today is too low to justify the ongoing regulation of the 1956 Consent Decree.").) Moreover, as we

pointed out in our Preliminary Statement (U.S. Prelim., tab 4, at 24), IBM affirmatively raised competitive and market issues in asserting that changed circumstances warrant termination. (See generally IBM Prelim., tab 2, at 17-27.)

The fact that IBM disputes the utility of market analysis gives it no excuse from responding to market-related discovery, for in "assess[ing] relevance in a given case, the court must view the matter in light of the specific claims and defenses asserted by the parties." Fletcher v. Atex, Inc., 156 F.R.D. 45, 48 (S.D.N.Y. 1994). Until the Court resolves that dispute with appropriate findings, the Government's discovery should go forward. Cf. Martin v. Valley National Bank of Arizona, 140 F.R.D. 291, 300-01 (S.D.N.Y. 1991) (defendant was entitled to discovery on a defense until that defense is "stricken" by the court).

B. <u>The Government's Discovery Is Relevant To Equitable Issues Raised By IBM's Motion</u>

The information and documents that IBM refuses to produce because they are "market-related" also are relevant to assessing the potential for harm that outright decree termination may cause to IBM customers, competitors, or other third parties. (Tierney decl., ¶20.) General principles of equity require this assessment in considering IBM's motion to terminate the decree, even if it did not implicate matters of antitrust policy. See

Fed. R. Civ. P. 60(b)(5). In this context, the discovery sought by the Government will assist in determining whether and under what circumstances it would be equitable to grant the motion in light of the fact that many entities have relied on the competitive conditions created by the decree. (Id.)

As we stated in our Preliminary Statement (U.S. Prelim., tab 4, at 46-47), the decree has created certain competitive conditions and has encouraged investment and reliance upon those conditions. The effects of decree termination on consumers and entities that have relied on the decree is relevant to and should inform the Court's exercise of its equitable discretion regardless of whether the Court undertakes to inquire as to IBM's ability to exercise market power in properly defined markets. Indeed, IBM seems to be in agreement on this point, for as IBM counsel has informed the Court: "[w]e said, I thought fairly clearly and specifically, what we think the issues are. And they do not -- they should not be read to say that there is no reason to look at the impact of vacating the provisions of the decree at which our motion is directed. That would be, frankly, quite silly a position to take. And we don't take it." (06/19/95 Tr., tab 22, at 19.) (emphasis added).

Consideration of the equitable interests of IBM's customers and others who have relied on the decree may require a sunset period before termination of the decree even if market analysis indicates that termination would not pose significant competitive risks. In the case of

the AS/400 marketplace, for example, the Government has concluded that while competitive conditions and equitable considerations do not warrant opposition to decree termination, a sunset period is necessary to allow customers to make orderly adjustments of expectations and plans, and to avoid causing undue capital losses to the entities whose entry into the AS/400 market the decree has encouraged and facilitated. (Tierney decl., ¶4.) Such an outcome would be entirely consistent with the law, for the Second Circuit recognizes the appropriateness of phasing-out an antitrust decree that no longer protects consumers, in order to protect investment made in reliance on a decree. See United States v. American Cyanamid, 719 F.2d 558, 567 (2d Cir. 1983), cert. denied, 465 U.S. 1101 (1984).

IV. IBM Should Be Ordered To Produce Requested Information And Documents Relating To Operating System Software

The Government's August 4, 1995, discovery requests expressly define the AS/400 and System/360 . . . 390 products to include IBM's operating systems software for the products. (Interrogatories and Requests for Production of Documents, tab 6, ¶I.4, II.26.) However, IBM has refused to produce responsive information or documents related to operating system software, based on a relevancy objection which in turn is grounded on the erroneous premise that the decree does not apply to software. (Tierney decl., ¶21; see also IBM May 10, 1996 Objections, tab 13 (as to Interrogatory 7, objection to request seeking information about IBM's policy relating to software licensing).) Regardless of whether the decree expressly applies directly to software, issues relating to the distribution and licensing of operating system software are highly relevant to this proceeding because a number of provisions of the decree enjoin IBM from exploiting any operating systems software market power to engage in economic discrimination against purchasers of computers.

A. The Decree Applies To Operating System Software

We previously have disputed IBM's contention that the decree does not apply to software. IBM's Chronology of the 1956 Consent Decree ("IBM Chron.") (dated June 6, 1995), tab 3, at 27. The decree applies to electronic data processing machines, or "EDPM," and electronic data processing systems, or "EDPS." The decree defines "EDPM" as machines or devices and attachments therefor used in or with an electronic data processing system (Decree §II (f)); software is most certainly a device or attachment under this definition. Further, the decree defines "EDPS" as any single working machine or group of intercommunicating machines that is affirmatively capable of performing the functions described in the definition, such as "entering, receiving, storing, classifying, computing, and/or recording alphabetic and/or numeric accounting and/or statistical data . . . ." (Id. § II (e).) So defined, EDPS includes operating system software because, as IBM has acknowledged, "computers simply do not work without software." (IBM Prelim., tab 2, at 21). Operating system software would also come within the meaning of parts for repair and replacement that IBM is required to supply to computer owners and maintenance service providers on a non-discriminatory basis. (Decree § VI(c).)

The fact that operating system software is colloquially distinguishable from the hardware aspects of a computer does not exempt it as a device or attachment for a machine that is used in or with a working EDPS. Likewise, the fact that operating system software may have come into use after entry of the decree does not provide a basis for IBM's contention. Indeed, the decree nowhere indicates that the words "device" or "attachment" should be limited to hardware products, or to products that IBM only marketed before the decree was entered. IBM concedes that an EDPM, as defined in section II(f), includes "anything that is part of an 'electronic data

processing system,'" as defined in section II (e). (IBM Chron., tab 3, at 27.) IBM thus admits that the decree applies to all IBM hardware and to all forms of peripheral devices (id.), even though, just like much of today's software, numerous types of hardware and peripheral devices did not exist in 1956. Further, IBM defended the government's bundling charges in the 1969 case (see Plaintiff's Statement of Triable Issues (dated September 23, 1974), tab 19, at 8-11) by pointing out the essential symbiotic relationship between hardware and software and how computer functions could be transferred between hardware and software.[3] Limitation of the decree to hardware not only would contradict the express language of section II(f), which on its face allows for no such limitation, but also would permit IBM to evade the decree simply by shifting computer functions from hardware to software.[4]

In defending its policy of giving away software against the Government's illegal bundling charges, IBM stated:

> IBM did not and does not now separately price that operating systems programming which is "fundamental to the operation of a system." . . . . Such programs are an integral component of any computer and are essential to render it capable of performing any useful task whatsoever.
>
> Moreover, operating system software is intimately intertwined with computer hardware during the design process. System functions are often transferred from hardware to operating systems software and back again in the design process as cost, function and technology evolve. As a practical matter, manufacturers must design an operating system together with their hardware.
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> . . . [G]iven the current state-of-the-art and sophistication, the computer hardware and operating system software are technologically and economically a single product. Customers and manufacturers alike treat the operating system as an integral element of the computer.

(*Pretrial Brief for Defendant International Business Machines Corporation* ("*IBM 1969 Pretrial Br.*") (dated January 15, 1975), tab 20, at 353.).

Largely to prevent this type of decree evasion, in an analogous setting, the Court of Appeals for the District of Columbia Circuit affirmed the District Court's conclusion, over the

IBM consistently has treated software as if it were covered by the decree. For example, in 1992, IBM charged ISSC, its computer services company, an additional $100 million than it otherwise would have charged had it deemed software exempt from the decree. (IBM's Memorandum in Support of Terminating the 1956 Consent Decree (dated August 24, 1993), tab 21, at 38). IBM recently advised the government that it treated software as if it were covered by the decree, in asserting that "while it may well be that the software transactions are not covered by the Decree, IBM has treated them as if they are." (Id. at 38 n.13).

Moreover, IBM has been unsuccessful in court with the argument that software is beyond the bounds of the decree. See Allen-Myland, Inc. v. IBM, 746 F. Supp. 520, 544 (E.D. Pa. 1990), vacated 33 F.3d 194 (3d. Cir. 1994). The court in Allen-Myland held that IBM violated decree § VII(d)(3), which prohibits IBM from limiting alterations in its computers, when it priced the additional copy of 3090 microcode necessary to split one large 3090 computer into two smaller computers in a manner that sought to eliminate such splits. Id. at 544, 546. The court specifically disagreed with IBM's contention that applying the decree to copyrighted software

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government's objection, that a provision in the AT&T consent decree prohibiting the Bell Operating Companies ("BOCs") from manufacturing telecommunications equipment also prohibited the development of software that is integral to telecommunications hardware. In *United States v. Western Elec. Co., 894 F.2d 1387, 1394 (D.C. Cir. 1990), the Court of Appeals explained:*

> *Indeed, because "firmware" circuitry has largely supplanted the more cumbersome vacuum tubes, wires and switches that formerly comprised the heart of many pieces of telecommunications equipment, the reading of section II(D)(2) urged by the DOJ would leave the BOCs free to perform the most significant design and development functions associated with the manufacture of telecommunications products.*

Id.

would go beyond the "four corners" of the decree. Id. at 544.[5]

Inclusion of operating systems software potentially is an important means by which the decree stimulates or facilitates competition in markets for EDPM and EDPS. For example, given such inclusion, § XV(b) of the decree requires IBM to sell operating system software licenses to all interested customers by preventing IBM from conditioning the sale of such licenses on the customer's purchase of IBM hardware, instead of used IBM or new or used plug compatible hardware. Customers would not have this protection if the software is not a device or attachment within the meaning of EDPM. In addition, § VII(d)(3), limits the ability of IBM to prohibit the attachment of used or plug compatible equipment to its operating system, and § VII(b) limits IBM's ability to require that customers even disclose to IBM the uses of their operating systems. And as noted before, § VI(c) requires IBM to supply operating system software, among other computer parts, to owners and maintenance service providers on a non-discriminatory basis.

B. The Decree Prohibits IBM From Implementing Operating System Licensing Or Maintenance Practices That Would Allow IBM To Avoid Its Decree Obligations

The Government's discovery as to operating system software is relevant regardless of whether the Court determines that operating system software is included within the product coverage of the decree. (Tierney decl., ¶23.) The decree prohibits IBM from implementing

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The court in *Allen-Myland* concluded that 3090 microcode, which IBM provides without extra charge as "Licensed Internal Code" with each computer, is a necessary element of a 3090 system, but is not in and of itself an EDPM as that term is defined in decree § II(f). *Id*. at 542. Thus, the court seems to have accepted the contention, as to 3090 microcode, that IBM argued with respect to operating system software in the 1969 case--that microcode is an integral and fundamental component of a computer that cannot be separately sold. *See supra,* n.3. Because IBM now separately licenses operating system software, it can no longer make this contention as to operating systems.

operating system licensing or maintenance practices that would permit it to avoid its decree obligations with respect to covered hardware products. IBM is required under § IV(c)(3) to establish such nondiscriminatory terms as may be appropriate for the sale of IBM computers. Thus, IBM cannot refuse to license its operating system to purchasers of IBM computers and it cannot discriminate against purchasers by charging them higher licensing fees than it charges to its lessees.

The non-discrimination provision of § IV(c)(3) applies to the sale of all new and used IBM computers and on its face it is not limited in applicability to sales made by IBM. By requiring IBM to license operating systems to purchasers of used computers, § IV(c)(3) makes competition from used computers possible, and provides an essential safeguard to the competitive viability of used equipment dealers. This section also fosters the overall purpose of § IV, which IBM concedes was to establish a market for used IBM computers. (IBM Chron., tab 3, at 29); 11/4/70 Tr. at 2-3 (tab 15 of U.S. Selected Docs submitted to the Court on April 3, 1995).) The value of a used computer is totally dependent on the purchaser's ability to obtain an operating system on terms that do not make acquisition of the computer an unattractive investment. Further, the price that a purchaser pays for an IBM computer will depend on the product's expected residual value to be recovered after the computer enters the used market. An interpretation of § IV(c)(3) that did not require IBM to provide operating system software licenses on a nondiscriminatory basis to all purchasers of IBM computers, regardless of whether the computer was purchased from IBM or a used computer dealer, would be contrary to the purpose of § IV in establishing a used computer market. A computer would have no residual value and would not even be expected to enter into the used market in competition with IBM

unless the purchaser could be assured that subsequent purchasers would have access to IBM's operating system software on a nondiscriminatory basis.

In addition, § VI(b) of the decree requires IBM to provide maintenance for owners of IBM computers on a nondiscriminatory basis for as long as IBM continues to maintain that type of computer. Because a computer cannot work without an operating system, IBM cannot fulfill its maintenance obligation unless it provides all owners of IBM computers access to its operating system software on a nondiscriminatory basis. IBM's obligation to provide operating system software on a nondiscriminatory basis pursuant to its obligation to provide maintenance to IBM computer owners would exist even if the court determines that IBM has no independent maintenance obligations for licensed operating systems under § VI(b).

V. IBM Should Be Ordered To Comply With Requests Relating To IBM's Disclosures Of Interface Information

A number of the Government's discovery requests seek information or documents relating to IBM's disclosure of interface information to users of its computers.[6] *As defined in our requests, an "interface" is a logical or physical interconnection or interaction that allows different computer products to interoperate with each other, while "interface information" refers to descriptive material that would enable a person to design a product to interoperate with IBM computer products. IBM has refused to produce the requested information or documents on the erroneous premise that the decree does not apply to interface information. (Tierney decl., ¶24.)*

See Interrogatory 12 (seeking descriptions of the interface information historically disclosed by IBM), Interrogatory 13 (seeking information on changes that IBM plans to make in the disclosure of interface information or in the licensing, enforcement, or assertion of rights under copyrights or licenses) and Document Requests 23, 24, and 25 (requesting documents relating to various aspects of IBM's interface information disclosures). (*Interrogatories and Requests for Production of Documents,* tab 6.)

Although the term "interface" does not nominally appear in any decree provision, it is within the reach of §§ IX(b)-(c), which require IBM to disclose to users the same information that it makes available to its repair and maintenance employees as well as information relating to the operation and application of IBM computers. The utility of IBM's computers is critically dependent on users' ability to operate the computers with other products that the users develop themselves or purchase from third parties. Many users devote considerable staff and resources to the sole purpose of developing or enhancing products to be used with IBM's computers. The information that IBM discloses pursuant to §§ IX(b)-(c), which shows how the computers are designed, how they work, how they are operated and how they are applied, clearly includes interface information that users need to design and attach products that will work with IBM computers. IBM's failure to provide such information would severely constrain the potential applications and operation of its computers. In this context, IBM's response to the Government's Interrogatories 12 and 13, that it has never disclosed pursuant to any decree obligation "what it considers to be 'interface' information" (as compared to the actual definitions of "interface" and "interface information" in the Government's discovery request), is unresponsive and misleading.

IBM has a longstanding practice of making interface information widely available to owners and lessees of IBM computers, including manufacturers of computer products that are plug compatible with IBM computers. IBM even defended itself against the charges in the Government's 1969 case by admitting:

> *IBM also publishes manuals which make available to other manufacturers the detailed interface specifications necessary for manufacturers to manufacture equipment which will communicate with IBM processing units and replace IBM equipment.*

(IBM 1969 Pretrial Br., tab 20, at 111.) Access to interface information can be essential to the competitive viability of a plug compatible manufacturer who uses IBM computers in the design and development of competitive compatible products.

Since § IX requires IBM to disclose interface information, the Government's requests for information about IBM's interface disclosure practices and possible changes in those practices clearly seek relevant information or information reasonably calculated to lead to the discovery of admissible evidence. (Tierney decl., ¶26.) IBM's assertion that it disclosed interface information for reasons apart from the decree does not answer the question as to whether the decree would now act as a constraint if IBM found itself otherwise free to curtail these disclosures. In any event, so long as there is a dispute as to whether the decree requires interface information disclosure, the Government's discovery should go forward. See discussion at 11, supra.

VI. IBM Should Be Ordered To Produce Responsive InformationAnd Documents Located Outside The United State

IBM generally has objected to the Government's discovery on the grounds that "they are not reasonably calculated to lead to the discovery of admissible evidence to the extent that they seek information located outside the United States." IBM May 10, 1996 Objections, tab 13, ¶ 6. Before explaining why this objection cannot be sustained on the basis of relevance, we note that to the extent that production of relevant foreign information imposes burdens on IBM, the Government has been and remains committed to reducing those burdens as much as possible. (See Tierney decl., ¶13.) We have offered to allow IBM to defer any efforts to produce responsive foreign material until we have examined IBM's initial responses, and we have informed IBM that any subsequent requests for foreign material would likely be much more

narrowly drawn given review of the initial responses. (Id. ¶32.) However, by failing to reach an appropriate agreement to allow the Government to reserve the right to seek enforcement of our discovery beyond the May 24 cutoff for motions to compel, IBM has forced the Government to move to compel before the parties have had an opportunity to address issues of burden that IBM may wish to raise. (Id. ¶¶29-34.) In any event, the Government is more than willing to consider any proposals that IBM may suggest in terms of narrowing or refining the scope of any of our discovery requests that may entail the production of information or documents outside the United States.

Before having completed review of IBM's initial responses, however, the Government cannot responsibly allow IBM to avoid completely the production of information from its foreign operations, because that information may prove to be critical to the market analysis and assessment of competitive conditions needed to resolve IBM's motion to terminate the decree. (Tierney decl. ¶28.) Information from IBM's foreign operations is likely to be highly relevant to questions as to defining the geographic market in which to assess IBM's ability to exercise market power. (Id.) Indeed, definition of the relevant geographic market presented major issues of contention in the Kodak case. 63 F.3d at 102, 105-09. In this case, the only market that IBM has thus far alleged is worldwide information handling. (Memorandum of Law in Support of IBM's Motion to Terminate the 1956 Consent Decree (dated August 24, 1993), tab 21, at 9.) Information from IBM's foreign locations may be uniquely relevant and necessary to test the validity of this alleged worldwide market and to determine the structure of any other appropriate markets. The Government is entitled to discover this information.

In addition to geographic market definition and structure, discovery of information from

IBM's foreign operations can provide significant insights as to whether the decree has constrained IBM from wielding market power. Since the decree does not apply to IBM's business outside the United States, comparisons of IBM's domestic and foreign pricing, profitability, and distribution and sales practices could be highly probative. Moreover, foreign discovery may be necessary to evaluate IBM's claims that the decree has imposed various costs on its domestic operations that it does not encounter overseas. (Tierney decl.,¶28). IBM has made other comparisons of IBM's businesses inside and outside the United States to suit its own interests, but it has not provided pertinent underlying details sought by the Government. (Id.) The Government is entitled to discovery of the information necessary to test these assertions. Without better certainty as to whether adequate evidence on these issues will be produced from IBM's domestic records, the Government cannot forego the right to seek relevant information from IBM locations outside the United States.

VII. <u>IBM Should Be Ordered To Produce Previously Deferred Information And Documents</u>

With respect to its partial responses to certain of the Government's requests, IBM has for the most part produced or promised to produce information or documents only to the extent they are found at certain of its headquarters locations. (Tierney decl., ¶31.) The Government was willing to accept these partial responses during the initial phase of its investigation, but expressly reserved its right to obtain additional responses to pending requests as the need arose and as the investigation progressed. (Id. ¶32)[7] Similarly, IBM has not produced any

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In its Objections to the Government's discovery, IBM repeatedly indicated that it had "fully responded . . . in accordance with the parties' agreement." In fact, the Government has not agreed to any limitations on the scope of any of our requests, other than permitting IBM to defer production of additional responses to requests for which it had made or promised a partial response. As explained above, we permitted the deferrals subject to our right to seek additional future responses to the extent necessary.

information or documents located outside the United States, although it is willing to provide information about foreign operations to the extent otherwise found in responding to our discovery. Again, we were willing to accept such a limitation on IBM's initial responses, but we reserved our right to request responsive information from foreign locations on an as needed basis. Accordingly, the Government permitted IBM broadly to defer production of all responsive information and documents that have not yet been produced or promised, subject to possible future recall.

In anticipation of the May 24, 1996, cutoff date for motions to compel responses to the parties initial discovery, the Government raised with IBM the question of how to treat the deferred documents. In an effort to narrow the discovery issues to be resolved by the Court, the Government offered to accept on a conditional basis IBM's partial responses and to allow unproduced responsive material, including all responsive material at IBM's foreign locations and all domestic locations that it has not yet searched, to remain deferred for the present time subject to any subsequent motion to compel. As proposed to IBM, continued deferral of all unproduced information and documents, would be conditioned on IBM's agreement that the Government not be bound by the May 24 deadline for filing a motion to compel discovery of the currently deferred material, in the event that we later ask IBM to submit supplemental responses. Under our proposal, the Government would have the opportunity to review the adequacy of IBM's partial responses before deciding whether to seek, if ever, any additional responsive information. We assured IBM that, except for good cause shown, we would not seek to rely upon the filing of any such motion to compel to alter any of the timetables set forth in the May 1, 1996, Scheduling Order. (Tierney decl., ¶33.)

Unfortunately, the parties were unable to reach agreement along the lines proposed by the Government, necessitating this motion to compel discovery of the responsive information and materials that up until now has been deferred. If this motion is granted, the Government is willing and prepared to meet with IBM to consider any issues that it may wish to raise concerning the scope and timing of additional responses.

VIII. Conclusion

For the foregoing reasons, the Government's motion should be granted and IBM should be ordered to produce all information and documents that it has withheld from the Government's discovery on the basis of its objections as to the relevance of market analysis, operating system software, or disclosures of interface information. In addition, IBM should be ordered to produce all responsive information and documents that previously had been deferred from production.

Respectfully submitted,

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N. Scott Sacks (NS-6689)