Issue 8.03 | Mar 2000

WIRED SPECIAL REPORT

Fear and Trembling in Silicon Valley

Even with an initial federal court finding that Microsoft is a monopoly, it takes real courage to stand up publicly to Bill Gates' empire - just ask any of the CEOs who have yet to come forward. John Heilemann tells the inside story of high tech's struggle to do the right thing.

Two weeks before Christmas, on one of those balmy, pale-gold afternoons that pass for winter in Northern California, a handful of Silicon Valley's most prominent executives and financiers held a secret meeting whose leitmotif was that rarest of concepts in the world of business: guilt. Needless to say, the topic was Microsoft.

Microsoft's culpability for an extravagant assortment of sins - venial and mortal, trivial and profound - has long been a favorite subject in the salons of the Valley, not to mention, more recently, the US Department of Justice and the E. Barrett Prettyman federal courthouse, in Washington, DC. But while Microsoft's redhandedness was the meeting's focus, the gathering itself was the product of a different brand of guilt: a guilt *trip,* to be precise; a guilt trip laid on the Valley by the government's trustbuster-in-chief, Joel Klein.

Even before Judge Thomas Penfield Jackson disgorged his searing findings of fact in the Microsoft trial, Klein had been laboring to line up support in the Valley for what would come next. With Jackson's findings, the trial's thrust would shift from crime to punishment, and Klein had an eye fixed firmly on the court of public opinion. If the DOJ were going to pursue severe sanctions against Microsoft, he would need the backing of Silicon Valley's leaders. Not backing for himself, but for serious remedies. And not subtle, clandestine, backstage support, but up-front, vocal, public support. The kind that shapes media coverage and editorial opinion; the kind that gets through to the man in the street; the kind that changes minds, and moves votes, in Congress. Klein knew that the remedy phase of the trial would be intensely political. He needed the Valley to make some noise.

What he got instead was a thundering silence. But now, after a month's worth of wheedling, cajoling, and badgering, a month of appeals to conscience, righteousness, and rational self-interest, Klein appeared at last to be making some progress. Assembled in the Mountain View offices of the software firm Intuit was a collection of Microsoft's fiercest rivals and critics, from Sun Microsystems CEO Scott McNealy and Oracle president Ray Lane to former Netscape CEO Jim Barksdale, Novell CEO Eric Schmidt (by phone), and, unsurprisingly in light of the venue, Intuit founder Scott Cook and Intuit CEO Bill Campbell.

For nearly two hours the debate was engaged. Should Silicon Valley's majordomos speak out on the subject of remedies? If so, how? Brashly or diplomatically? Collectively or individually? And, of course, what should they say?

For Joel Klein and his team, the mid-December meeting at Intuit was a signal episode in a prolonged struggle, and, perhaps, a turning point. From the beginning of the saga of *US v. Microsoft,* the reluctance of the Valley and the rest of high tech to talk - out loud, on the record - about Redmond's behavior has been a source of understandably intense frustration within the DOJ. With a great deal of doggedness and even more luck, the government had managed to fill its dance card of witnesses for the trial. But just barely. And for every executive who was induced to testify, there were countless others with potentially incriminating information to impart who refused to come forward. Too risky, they said; Microsoft could hurt them in too many ways.

As the trial played on, the DOJ's lawyers tried to comfort themselves with a hopeful refrain. Two words: "Just wait." Microsoft's partners, customers, and competitors might be too timid to speak up while the outcome of the case remained in doubt. But once the initial phase of the trial was over and Judge Jackson had issued his ruling - a ruling that everyone who had devoted even an iota of attention to the trial-cum-bloodbath assumed would run hard against Microsoft - well ... just wait.

"If Jackson comes down big in our favor," a senior government lawyer told me last February, "all these guys who are afraid to talk now are going to be beating down the doors and lining up in the halls to testify in the remedy phase."

The sweeping and magisterial document issued in November by Judge Jackson was not, strictly speaking, a ruling. Yet the findings of fact, *these* findings of fact, were the next-most-telling thing. There could hardly have been a more lucid indication that the final ruling, due probably in April or May, will deal a harsh blow to Microsoft. Nor could there have been a more convincing testament to the ability of the Justice Department - about which the Valley, on the basis of past screwups, had deep doubts - to take on the world's most valuable corporation and more than hold its own.

Given all this, and given the sight of Microsoft staggering about in the aftermath of Jackson's findings like a dazed and headless beast, and given the chatter in the air about chopping the beast into two or three or four or six prime fillets, it was reasonable to expect that Klein would get what he so desperately desired. To expect that the titans of the new economy would be emboldened enough to venture opinions as to what should be done about "the Microsoft problem" - opinions they express privately in rants, tirades, and diatribes - in voices well above a whisper.

A reasonable expectation, perhaps, but dead wrong. In fact, in the weeks after the release of the findings of fact, Silicon Valley seemed transformed: from the Valley of the Dollars to the Valley of the Dullards. Amid the reams of paper, buckets of ink, hours of tube time, and millions of bits devoted to the Microsoft case, no more than a few lonely instances could be found of a high tech high roller speaking his mind on the subject of remedies.

It was not for lack of effort on Joel Klein's part. At the end of October, less than two weeks before Jackson's report was delivered, Klein paid a visit to Silicon Valley. In the past, Klein and his team had poured into the Valley to construct their case: to unearth evidence, hunt witnesses, collect tips, leads, leaks, and the occasional confidential white paper. Now, with Jackson's findings apparently imminent, Klein slipped out of his lawyer's garb and into that of a politician rousting his constituents as election day draws near. In a series of back-to-back meetings over a Sunday and Monday with more than a dozen of the Valley's ranking CEOs and venture capitalists, Klein presented his arguments calmly but urgently. Repeatedly he laid out the scenario he believed was likely to unfold. If Jackson hammered Microsoft, and especially if he deemed it to be a monopoly, Klein expected a tornado of spin to come twisting down from the great northwest. Klein predicted - correctly - that the Microsoft line would run something like this: Well, yes, sure, maybe we are a monopoly, but we're an aging, archaic, outmoded monopoly, with a stranglehold on an aging, archaic, outmoded technology. After all, in the age of the Net, who really cares about the PC desktop, anyway?

Klein implored the Valley guys to counter that spin. He asked them to make the arguments that market forces and new technologies were patently insufficient to restrain Microsoft's power. According to executives who met with Klein, he studiously refrained from encouraging them to support any particular remedy or type of remedy - structural, behavioral, or a mix of the two. Instead, Klein repeatedly invoked a vaguer phrase: "significant remedies." Klein left it up to the executives to decide what that meant. The crucial thing, he stressed, was to please, please say *something.* Anything.

"Joel is very political," one CEO told me. "He knows that if he lets Microsoft define the terms of the debate, he loses."

Despite Klein's intentional obliqueness, many of the executives came away with the distinct impression that he favored splitting Microsoft up, one way or another. "How do I get that impression?" a software executive said to me. "I get it because Joel only asks my opinion on structural remedies. Any time a behavioral remedy comes up, he looks bored."

That impression has only been strengthened in the weeks since Jackson's findings. In January, a flurry of leaks to the press suggested that the DOJ was indeed on the brink of endorsing a breakup. Behind those reports was the work of Robert Greenhill. In early December, the DOJ had hired the longtime Wall Street dealmaker to study the financial aspects of various remedies and offer a recommendation. In short order, Greenhill hit the ground in the Valley, impressing everyone he met as a man of clear purpose. "By the time he got to me, his mind seemed made up," one prominent Valley figure told me. For many months, one of the most dramatic remedies bandied about the halls of the DOJ was the "Baby Bills" approach: splitting Gates' firm into a number of mini-Microsofts, each with identical intellectual property. According to people who spoke with him, Greenhill indicated that he favored a slight variation on that theme, known to insiders as the slice-and-dice approach: divvying Microsoft into three separate operating-system companies, and leaving its application-software and Internet businesses to comprise either one or two additional companies.

As Greenhill's views took shape, Klein continued to work the phones, pleading with the Valley to do the right thing. "Joel is really born-again on this," one CEO said. "He's like Paul Revere trying to rally the troops." In truth, he's been trying to do more than that. To a handful of people with whom he has spoken, Klein suggested that he was looking for a major personage in the industry to be a public face for "significant remedies," making the case in the media that reining in Microsoft requires more than a judicially administered rap on the knuckles. And Klein wasn't looking for just any spokesman; he wanted a spokesman of a certain type. "Joel was looking for a poster boy," this CEO said. "A poster boy who isn't Larry or Scott."

The fact that Klein doesn't consider Larry Ellison, the CEO of Oracle, to be the optimal front man comes as no big surprise. Ellison is seriously over the top, thoroughly unpredictable. He's also a man who, for all the transparent joy he derives from tweaking Bill Gates, has played a remarkably limited role, publicly and privately, in the antitrust battle. Klein's avoidance of Sun's CEO, Scott McNealy, is somewhat more complicated. Though their worldviews could hardly be more different - Klein is a Clinton Democrat, McNealy an Ayn Rand Libertarian - for many months their relationship was cordial, respectful. McNealy thought highly of Klein, and was amply impressed with his handling of the case. And Klein was grateful for McNealy's famously big mouth; for the fact that, almost alone among Valley CEOs, he was willing to talk (and talk) publicly about what should be done to Microsoft.

The trouble, however, is that McNealy's position on remedies has been rather like Microsoft's defense was in the trial: loud, energetic, multiplicitous, internally inconsistent, and maddeningly all over the map. In the months before the trial started, McNealy was prone to putting forward proposals designed mainly for shock value. "We should shut down some of the bullshit the government is spending money on and use it to buy all the Microsoft stock," he told me in 1997. "Then put all their intellectual property in the public domain. Free Windows for everyone!" Once the trial got rolling, McNealy switched tack, embracing the idea, through Sun's chief counsel, Mike Morris, of the Baby Bills approach. Then, in December 1998, McNealy informed his board of directors that he was changing course again. His preferred remedy was no longer breaking up Microsoft, but banning Microsoft M&A: no takeovers, no minority investments, no joint ventures for the foreseeable future.

McNealy's shift caused deep unhappiness among certain Sun executives and board members. So why did he do it? "Scott had himself a little epiphany," a lawyer close to Sun said. "Today, Microsoft is the number one operating system company and Sun [with its brand of Unix, known as Solaris] is the clear number two. But if Microsoft is broken into three OS companies, Sun immediately drops to number four. And if Microsoft is broken into six OS companies, Jesus, Sun falls to seventh. The more McNealy thought about it, the more keeping Microsoft in one piece seemed like a pretty good idea."

Good or bad, the idea didn't last. "Scott has changed his mind again - hopefully for the last time," a Sun insider said not long ago, sighing and laughing in one weary breath. At a Sun board meeting last November, just a few days after Jackson's findings and nearly a year after McNealy's initial flip away from advocating the Baby Bills scheme, Sun's CEO told his stunned directors that he had flopped once more. The scope, the onesidedness, and the cogency of Jackson's findings - along with press coverage suddenly suggesting that a breakup was not only possible but plausible - had convinced McNealy that, despite its perils for Sun, the slice-and-dice solution was the way to go. He also floated a new, exquisitely McNealyesque behavioral remedy: Just as Michael Milken was banished from Wall Street for his crimes, Bill Gates and Steve Ballmer should be "disbarred" from the software industry for theirs. "Scott knows it'll never happen, but he can't help saying stuff like that," the Sun insider said. "It's just so ... *Scott*."

Not surprisingly, Scott being *Scott,* amusing as it is, has put something of a strain on his relationship with Klein. "Joel would probably have kept his distance from us anyway, because we seem like we have an ax to grind," a Sun executive said. "But there's no question Scott has hurt his credibility with Klein; they don't talk that much anymore." A person who speaks with both McNealy and Klein remarked dryly, "Joel thinks that Scott doesn't - how to put it? - contribute positively to the quality of the conversation."

Klein's search for spokesmen who aren't McNealy or Ellison wasn't a total washout. A vanishingly small and faintly predictable roster of Valleyites enlisted. Jim Barksdale was one of them. Mitchell Kertzman, the former CEO of Sybase and now the CEO of Liberate Technologies, was another. Maybe the most impressive was Bill Campbell, the boss of Intuit. Campbell, a former college football coach and a highly regarded leader in the Valley, has an assortment of bruises from butting heads with Gates. In the 1980s, Campbell worked for Apple and helped launch the Macintosh, which depended on Microsoft applications to find a place in the market. Then he was the CEO of the doomstruck pen-computing company GO, whose executives, Campbell included, contend that they suffered at Microsoft's hands many of the same predatory and exclusionary business tactics enumerated so vividly in Judge Jackson's findings of fact.

Yet, when the government first approached Campbell about having someone from Intuit testify in the trial's initial phase, he wanted no part of it. He regarded the DOJ's lawyers as hopelessly overmatched - "I told them, the Bill Neukoms of the world are going to cream you government pantywaists" - and he felt that participating in the case would be nothing but a distraction for Intuit. Eventually, though, Campbell came around. Now, with the DOJ having proved him wrong about its competence, he feels morally obliged to "stand up and be counted." Campbell is a structural-reform guy. He hasn't decided yet which of the various proposals he endorses, but says that any behavioral remedy (such as opening up the code to Windows) will be too easy for Microsoft to circumvent.

The strength of Campbell's convictions was also borne out by his willingness to serve as host of December's anti-Microsoft summit. Organized by a clutch of Klein's Silicon Valley allies who have gone to inordinate lengths to keep their names secret, the meeting produced a fair degree of consensus and a fairly ambitious agenda. The attendees agreed that they were all in favor of structural reform. They agreed that they would launch a quasi-formal campaign to push such a remedy, a campaign with a quasi-official leader - Mitchell Kertzman - and, perhaps, a staff and a budget. The companies involved might step up their political donations, to offset the millions of dollars that Microsoft is alleged to be pouring into Republican campaign coffers to sway opinion on Capitol Hill. The campaign's enlistees would focus on public persuasion, speaking to editorial boards, reporters, and interested politicians about remedies. There was even talk of hiring an executive-search specialist to hunt through the rosters of former employees of PC manufacturers in search of potential anti-Redmond whistle-blowers.

A fine plan. Will it actually happen? Remains to be seen; since December, no concrete steps have been taken to implement the group's ideas. More to the point: Even if the effort does pick up steam, will it change anyone's mind? "The problem with the meeting was that it was just all the usual suspects," one of the usual suspects remarked. If the campaign germinated that day at Intuit is to avoid being written off as just more whining and self-interested ax-grinding from the Valley's anti-Microsoft mafia, its members will need to summon a broader chorus in favor of structural remedies. A chorus, that is, of *unusual* suspects.

As it has been for Klein, the task of persuasion will not just be uphill but virtually vertical. Consider the PC manufacturers, who watched during the 1990s as Microsoft (and Intel) gradually sucked the profitability out of their business, and as their role was transformed from proud innovators to indentured servants. For months last winter Joel Klein labored to convince Ted Waitt, the chair of Gateway, to testify in the trial. Waitt is young, hip, ponytailed, iconoclastic, and blindingly wealthy. His firm's relationship with Microsoft is well known to be contentious, if not outright hostile. As Waitt told one of Klein's intermediaries, "Gates already hates my guts." But would Waitt testify? No. Has the release of Jackson's findings changed his mind? Apparently not. Waitt remains as silent as a church mouse - a young, hip, ponytailed church mouse - when it comes to remedies.

Or consider Eckhard Pfeiffer, the former CEO of Compaq, and a man who probably knows where as many Microsoft-related bodies are buried as anyone in all computerdom. Pfeiffer no longer runs Compaq; he is no longer dependent on Microsoft for his wealth or his health in any way. Does he talk? You must be kidding. Or think of Lou Gerstner, the CEO of IBM, by far the largest and most venerable computer company in the world, and a man who is said to have told Scott McNealy, "You go ahead and tilt at those windmills, son. I'll watch." And let us not even breathe the names of the vaunted venture capitalists of Silicon Valley, the financial masters of the digital universe, who have spent countless hours complaining privately to Klein about how Microsoft's rapacity poses a threat to the

Valley's investment climate - a climate that, to the untrained eye, seems fairly robust these days. If the threat is real, the time has come to explain the paradox. How many VCs have piped up and done so? Not a one.

"It's all completely predictable," one of the Valley's most influential men said to me recently. "People hear all this talk about the post-PC world and they buy this line that Microsoft's power is waning, and it's just not true. People have no idea how much power it still exerts." He went on, "Ted Waitt needs access to Windows 2000 as soon as his competitors have it; he can't afford to say anything that would jeopardize that. Eric Schmidt needs access to Microsoft APIs to make Novell's stuff work with Windows; he isn't going to mess with that. Without Microsoft Office, Apple is dead. Dead. Is Steve Jobs going to risk losing Office? C'mon."

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