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Microsoft

July 14, 1995

Mr. James R. Miller
IBM Corporation
P.O. Box 1328
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Dear Jim:

Mark Baber and I met with Joachim Kempin and Jan Claesson today to discuss your phone call and the issues that have surfaced in the Windows audit.

To make sure Mark and I understood your positions on the issues raised, I want to summarize today's phone call between you, Scott Palka (Ernst & Young), and Mark and me.

1. GTSI computers. Although IBM stated in a letter of 1/26/94 that you would provide Microsoft with an updated list of GTSI model numbers, the letter dated 7/12/95 from Scott Palka stated, "it does not appear that these model numbers were included in a designation to Microsoft." Your position is that all GTSI models qualify for the "per system" rate, whether or not they were designated as "per system" models.

2. Model designations. Section 9.22 of the Windows license states that IBM may elect to pay a per-system royalty by designating a model to be "per system" in writing to MS. "IBM shall provide notice of the foregoing elections to MS before each four (4) quarter period commences (or in the case of newly introduced model numbers, before the end of the first quarter of such four (4) quarter period)." A letter from Irwin Drucker, dated May 12, 1993 and signed by Deb McFarlane of MS, clarifies that "the four consecutive calendar quarter period is not required to commence on the first day of that respective calendar quarter." Most letters from IBM designating models as "per system" include effective dates. Your position is that regardless of the date of the notification letter or stated effective date in the letter, designated models should be at a "per system" rate from date of first shipment, whether or not that was prior to the designating letter.

3. Designation Expiration. Although both the Windows license and the May letter refer to the "four quarter period," you take the position that the designation is for the "life of the product." IBM has paid "per system" royalties based on that position.

4. Administrative Errors. The audit has revealed that some models were not designated as "per system" due to apparent typing errors. Your position is that these errors should be ignored.

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GOVERNMENT EXHIBIT 2370
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In today's phone call, you stated your feeling that MS is not accepting the "spirit of the agreement," that you think you may need to stop the audit until those issues are resolved, and that, due to these open issues, you are not sure you can sign the license for Windows 95 at this time.

Audit fieldwork is an objective fact-finding process that audits compliance with the terms and conditions of the agreements. Auditors should not be distracted by the "intent" of a contract, which is neither factual nor auditable. Therefore, it is essential to conclude the audits and review all findings prior to attempting to resolve the issues the audits raised.

In light of the reporting problems uncovered, as well as frequent late reports and adjustments, we are very concerned about your threat to stop the audit. It has been 9 months since you were first notified of our intent to audit IBM, and further delays are untenable. We expect all audits to be completed and reports published prior to September 16, 1995. At this point, we have serious reservations about your ability to report correctly under the more-stringent reporting requirements of the Windows 95 contract. We look to the audits to provide adequate assurance that, indeed, you will be able to comply with those requirements.

When we have had time to review Ernst & Young's audit reports, we will address all issues that arose from the audits and will certainly involve management in the process of resolving those issues.

Very truly yours,

Nell Miller

Nell Miller
OEM Controller

cc: Bruce Claflin, IBM
Jerry Casier, IBM
Joachim Kempin, Microsoft
Mark Baber, Microsoft
Scott Pallos, Ernst & Young