

November 9, 2023

Dear Members of the CMA:

CISPE welcomes the CMA's opening of a formal investigation into the supply of public cloud infrastructure services in the UK. Especially important to our members is your decision to investigate the unfair licensing practices imposed by several legacy software providers, in particular Microsoft. Not only are these well documented in the Ofcom Report, but they have been highlighted in several recent market studies.

These practices have a significant and ongoing foreclosure effect for customers and providers operating in the UK and across Europe in the cloud infrastructure market.

Although they are pernicious and wide-ranging, we believe that they are relatively straightforward to remedy with well-tested anti-trust measures. As such, they represent 'low-hanging fruit' that can swiftly deliver major benefits to the entire UK cloud sector and its customers. Together with our UK-based members, we stand ready to meet the CMA to provide further evidence of the above practices and of their foreclosure effect on the cloud infrastructure services.

Similarly, we are prepared to discuss and fine tune the remedies proposed by CISPE members which are limited to targeted contractual changes and would be fast and effective in addressing the unfair practices for UK customers, consistent within the potential remedies contemplated by the CMA, should the existence of adverse effect on the competition in the cloud market be established.

Today's deadline for submission to the CMA also marks a symbolic anniversary: one year ago, exactly on November 9, 2022, CISPE filed its complaint against Microsoft with the European Regulators, AZURE II, of which a non-confidential version is attached to the present filing (see [\gg]).

Unfair software licensing has significant adverse effect on competition in cloud services

In our view, the licensing issue has the most impact on cloud users and providers, and it is no coincidence that it is central to the four recent anti-trust complaints lodged at EU level against Microsoft unfair and discriminatory licensing practices. One of these EU-level complaints (AZURE II) was lodged by CISPE. ([%])

In contributing to the CMA investigation, we share some of the examples and practices covered in the CISPE anti-trust complaint to illustrate how Microsoft bundles and ties it dominant productivity products to force people into its own cloud or uses discriminatory terms to raise costs for businesses when they select cloud infrastructure from other suppliers.

The practices and examples are also documented in the first study by Prof Frederic Jenny at the end of 2021. (see $[\infty]$)



CISPE and its members have documented numerous examples of how such unfair practices foreclose competition on the cloud market.

They range from:

- customers prohibited from running the software they have purchased on competing cloud infrastructures offered by Listed Providers;
- through additional charges for security updates which can multiply the price of a given software application by a factor of ten (over several years);
- to degradation (or removal) of certain software features and functionalities without technical reasons when such software applications are used on competing cloud infrastructures that do not belong to the software application publisher.

A second and more recent research report from competition expert Professor Jenny (funded by CISPE, see $[\ll]$) suggests that additional costs or surcharges related to these practices add billions to the cost of moving to the cloud for businesses across Europe, including in the UK.

Recent unilaterally offered changes have not solved the issue. The withdrawal of the first antitrust complaint (Azure I) reported by the press did not correct the unfair practices.

Microsoft's recent changes to its licensing terms do not address key licensing issues outlined in our complaint to the European Commission and identified by several market studies including that of Ofcom. These unfair practices, including Azure's self-preference and discrimination on software pricing and features, continue to harm customers despite minor concessions made by Microsoft, with respect to the customers using cloud infrastructure from Listed Providers.

Similarly, the withdrawal of the first AZURE I by the three original plaintiffs (there is no official statement but only press articles on the withdrawal of the Azure I complaint or on the scope of the concessions secured by the plaintiffs) did not correct the unfair practices, at least not for companies that did not enter into private agreements with Microsoft.



On this basis and in response to Ofcom's questions on the same dated June 26, CISPE also provided specific answers to Ofcom's questions on July 25, 2023. (see [\gg])

Discriminatory pricing continues to restrict choice for UK customers. Some concrete examples Microsoft continue to insist that this is purely a commercial matter and that there are no concerns

over its pricing, citing the changes that it made in October 2022 to its CSP-Hoster programme "in response to European CSPs"; and claiming that European cloud infrastructure providers are 'happy' with these revised license terms. To the contrary, rather than being 'happy' with these changes, many of our members who are indeed also CSP-Hoster programme participants, feel they do not address their voiced concerns and have no choice but to participate. These same members have been instrumental in pointing out the discrepancies in Microsoft's figures and continue to call for formal investigations to achieve fair pricing and licensing terms.



CISPE has demonstrated how Microsoft uses price discrimination practices in its software licences to increase the costs of its competitors, thus penalizing companies willing to use the cloud infrastructures of competing providers. These practices, including Azure's self-preference and discrimination on software pricing and features, have continued despite the changes announced by Microsoft.



More recently, CISPE and its members have responded to requests for information from the Commission, providing additional evidence on this occasion.



For their part, the members of CISPE have provided new evidence corroborating the abuses denounced in the complaint, as summarized in the attached document. [%]:

- A member of CISPE performed a comparative price analysis and found that the purchase price for a SQL Server Enterprise Edition license for a 32-core VM is lower when that license is acquired from Azure than when it is purchased under the SPLA (i.e., the Competitive Service Provider License Agreement). As a result of these price discriminations, this CISPE member was able to calculate that the SPLA was about 20% more expensive than what an end customer would pay by using Azure's services directly. This pricing, which is far from constituting a simple "mark-up" on the prices charged by Microsoft for its software, does not include the additional costs imposed to access security updates and "patches" ("ESUs") which amount to 100% of the price of the software purchase license, payable each year. The same ESUs on Azure are provided free of charge to Microsoft's direct customers.
- Another CISPE members explained that they were providing Microsoft's products (productivity software) at a loss to their customers who also used their infrastructure services. Microsoft makes significant (20%+) annual increases in the cost of software productivity licenses purchased under SPLA and in most cases, members are unable pass on these increases to their customers. Doing so would risk of the latter leaving for Microsoft where the same productivity software is offer at a much lower price. Thus, the Azure cloud infrastructure services becomes increasingly more financially attractive than those provided by the CISPE member. One CISPE member explained that its costs were higher than the price charged by Azure to its customers, so that even if it allowed itself a zero margin, it would not be able to compete.
- Another member of CISPE provided a list of customers lost due to Microsoft's pricing-related abuses, estimating this loss to be more than £17,000,000 in total in the past 3 years. Other members also explained that the financial data they had provided was only for existing customers, without prejudice to customers they had lost because of Microsoft's abuses, including licensing.
- Another CISPE member also explained that their customers could not purchase Windows
 Client and Microsoft 365 licenses directly from them or use their existing licenses on their own
 cloud infrastructure due to the exclusion of the "listed Providers" by Microsoft (Listed



Providers include: Google, AWS, Alibaba and ironically, Microsoft). They also indicated that Windows 10 and 11 were not available under the SPLA, which made it very difficult to provide a Desktop as a Service (DaaS) offering that competes with Microsoft's.

• In parallel, the latest study by Professor Jenny (July 2023) demonstrated, by comparing the cost of licensing a Microsoft product in an independent cloud environment, with the cost of the same software running in Microsoft's Azure environment, that European companies pay an additional "tax" of approximately 28% equating to several billion euros of excess payments each year to be able to use the software they own in an infrastructure competing with Microsoft's. These losses are detrimental to growth, innovation, and faster digital transformation of the UK economy.

Despite all these elements, and even though Microsoft has publicly acknowledged the existence of 'unintended consequences' of its licensing practices, no serious negotiations have taken place with CISPE over the past six months, as Microsoft has never seriously considered or taken a position on the materiality of the remedies proposed by CISPE.

To date, there has been no negotiation with Microsoft

Microsoft claims it is engaged in "constructive settlement negotiations with CISPE" on behalf of its members. This is even mentioned in the OFCOM Report. Yet it is inaccurate and misleading. Since CISPE's filing of its EU anti-trust complaint, three meeting have taken place with Microsoft. The first meeting was to present the Microsoft proposed changes to its licensing practices and a settlement offer to CISPE and its companies. This offer and the proposed changes were part of the October 2022 creation of Microsoft CSP-Hoster programme "in response to European CSPs". It was far from the mark and did do not address any of the key concerns and discriminatory practices alleged by CISPE.

The second was a 30' courtesy introduction with a senior Microsoft manager designed to dissuade CISPE from issuing a media statement on the lack of engagement by Microsoft while Mr Brad Smith, the President of Microsoft, was in Brussels evangelising European lawmakers on AI; the third and last meeting was an 'information exchange" to answer technical questions and clarification on the settlement requirements that CISPE members had prepared collectively and sent to Microsoft in May 2023. At no moment in any of these instances did Microsoft to take a view, provide any reaction or make any proposal relating to CISPE's requirements.



CISPE's proposed remedies would be, fast and effective for UK customers. They also fall squarely within the potential remedies already contemplated by the CMA in the cloud service market

Most importantly, perhaps with one exception, the actual changes sought by CISPE companies in the Microsoft unfair licensing practices require no engineering effort or changes to the existing software products. Except for the creation of a privacy-friendly auditing tool, Microsoft could fix all the problems and eliminate all the discriminatory practices at the heart of CISPE anti-trust challenge, literally by a snap of their fingers and without writing a single line of software code.



To illustrate this point, we include with this note the consolidated CISPE settlement requirements that we presented to Microsoft in early summer 2023 (see [%]). These requirements were crafted in close consultation with all affected CISPE members and represent an easy and effective way for Microsoft to lift its discriminatory licensing restrictions and address regulatory concerns. Microsoft has made no response to these detailed suggestions other than to dismiss them out of hand. Claims that remedies will be complex, hard to implement and destructive to Microsoft's core business model are untrue. After all, Bring Your Own License was Microsoft's business model up until October 2019.

CISPE members and their customers believe that simple remedies, auditable by any independent auditor, can be extended to other legacy software providers who impose similar discriminatory and self-preferential terms and conditions. Thus, they can deliver fast and far-reaching benefit to all cloud customers in the UK.

Regulatory pressure will be effective, and is necessary, in eliciting change

We contend that absent appropriate enforcement or judicial redress, nothing in the current behaviour indicates that these unfair self-preferencing practices will disappear in the future, and instead infer that similar practices could be extended to other dominant software products of the firm including, for example, Al-based software services and future cloud-based gaming applications.

The concessions extracted by the CMA from Microsoft during negotiation on the Activision acquisition, show that, when faced with regulatory pressure, Microsoft can be persuaded to make concessions to improve the contestability of the cloud sector.

Another much recent example of this behavioural pattern can be found immediately following the opening of the CMA formal investigation into the supply of public cloud infrastructure services: It is no coincidence that, in the wake of the opening of the CMA investigation - Microsoft swiftly responded to the letter by CISPE (see [\gg]) documenting the lack of negotiations and contacted CISPE again with a view to a future meeting.

The CMA has, therefore, a golden opportunity to end unfair software licensing practices for the benefit of all cloud customers in the UK.

We look forward to meeting the CMA and to provide further evidence of the above practices and of their foreclosure effect on the cloud market to the detriment of all customers in the UK and globally.

Sincerely Yours, Francisco Mingorance [≫]





Francisco Mingorance | Executive Secretary & Gaia-X founding Board Member 87 Avenue Louise, 1050 Brussels-BE | []

https://cispe.cloud | EU Transparency Register | TVA BE 0666.662.093

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