From: Kelly, Thomas M._SupMgmt [Kellytho@Gateway.com]
Sent: Wednesday, January 27, 1999 1:04 PM
To: Gayle McClain; Kelly, Thomas M._SupMgmt
Cc: Flanary, Mike; Rob Young (OEM)
Subject: RE: REQUIREMENTS

Importance: High

Gayle,

From before the apps negotiation began we have consistently indicated the need to have a very competitive royalty rate on Works Suite. Back then we were willing to look at an $8.00 dollar price point. We very reluctantly agreed to $12. When Richard came into the negotiations the $12 was reneged upon and we landed at $17 dollars. We had no option to walk form some amount of Works Suite. It was a little like having a gun to our heads. AUPs continue to drop. If we are going to cover all consumer systems we must have a $5.00 price point. Barring that, going with the agreed upon volume of Works Suite at $17 is the only option we see. There is a large opportunity on the low-end but our final solution cannot be uncompetitive as to price or content. On both counts we need the best in the industry. If moving a non-essential component of Works Suite gives you some other justification to provide us a competitive price and competitive content we will look at that. All discussions to date have been about Microsoft constraints, not Gateway requirements, which I have not seen change.

As regards the global content, Gateway has consistently asked and required this. What I have seen happen over the past 8 months in Europe and Australia on the Office products is not moving Gateway in the proper competitive direction. Again, these were Microsoft issues (separate agreements and pricing) not Gateway objectives. Microsoft and Gateway will both win if we work a truly competitive solution that meets Gateway requirements.

Thomas

-----Original Message-----
From: Gayle McClain [mailto:gaylemc@microsoft.com]
Sent: Wednesday, January 27, 1999 12:16 PM
To: 'Kelly, Thomas M._SupMgmt'
Cc: Flanary, Mike; Rob Young (OEM)
Subject: RE: REQUIREMENTS

I'm confused by the low-end apps information below. It is not consistent with what we have discussed to-date. For example, GW has now added a requirement for a global agreement.

When will the requirements be solid? Who owns this deal on GW's side? Why would GW confirm the W/S $17 for 500k unit deal when you're asking for something different in this space below?

I am totally confused.

-----Original Message-----
From: Kelly, Thomas M._SupMgmt [mailto:Kellytho@Gateway.com]
Sent: Wednesday, January 27, 1999 9:05 AM
To: Gayle McClain
Cc: Flanary, Mike
Subject: REQUIREMENTS
Importance: High

LOW-END

Gayle,

As I have indicated, we are ready to exercise our option on the 500,000 unit Works Suite commitment at $17. In order to consider a complete low-end offering below are our requirement

OFFICE FAMILY LOW END REQUIREMENTS
FOR RECONSIDERATION OF THE LOW-END

- Term: 1 year
- Content: Works Suite content
- Volumes: TBD
- Territory: Global
- Price: $5.00, No up-lift rates for foreign language versions
- License: Per system consumer pre-loaded. Option for add-on and post system sale sales.
- Internal Use: A no charge, non-exclusive license to use 2000 copies of the Software for Gateway's internal use and demonstration purposes.
- Sales Support: MS to furnish Gateway at no charge, with sales aids, product info, brochures etc. which MS generally makes available to other OEMs.

Training: Sales and Technical Support Training to be included at no additional charge

COUNTRY STORES

MS has suggested pricing of $119, $119, $119, and $169 respectively for the bundles with an across the board 40% discount (royalty only) off this suggested price.

Typical distributor pricing for the title mix we are dealing with is 20-25% off a suggested retail price. The publisher/manufacturer also typically provides the following:

- marketing co-op funds
- price down support
- COGS & distribution
- product support
- returns management

When we factor COGS and support only into the equation this deal becomes no better than a distribution agreement. If we factor in the other incentives and costs of marketing and management of the product this becomes less than desirable.

We have reviewed PC Data information and believe that Gateway is a significant marketer in terms of ship share and revenue for many of these Microsoft titles.

We have agreements in place with other publishers which allow us to market consistently to our customers at the point of PC purchase or after purchase with the same business terms. The launch of Microsoft titles will impact other current offerings.

If MS needs to protect channel pricing, as there proposal states, then we propose that we index royalties in accordance with any end-user pricing change. example: If the end user price for after PC purchase is 20% higher (than with a system) then Gateway's royalty increases 20% over the current royalty.

We propose a compromise to IMG to meet somewhere between their 40% number and the "indexing model" can we work this out?