

SCO v. Novell

SCO and Novell's
Motions for Partial
Summary Judgment
on Novell's Fourth
Claim for Relief on
APA para 4.16

**UNITED STATES DISTRICT COURT
DISTRICT OF UTAH
Civil No.: 2:04CV00139**

Novell's Interpretation Would Allow It to Destroy the Value of the Business Santa Cruz Acquired

Despite the intent of the APA to transfer “all of the Business” to Santa Cruz, Novell claims the unfettered right to:

- Allow any and all SVRX licensees to use, disclose, and profit from the SVRX source code without any protection or compensation to SCO.
- Waive any material breach of any contract related to the SVRX source code, including Software and Sublicensing agreements.
- By the foregoing, also effectively destroy the value of the UnixWare source code and licensing business, which are built upon the prior SVRX technology.
- Extinguish the rights Santa Cruz bargained for and obtained in clear provisions of the APA, including all rights and ownership in the UNIX technology, rights under the source code contracts, and rights to defend the UNIX intellectual property.

APA Was Intended to Transfer All Rights and Ownership of UNIX and UnixWare to Santa Cruz

- “It is the intent of parties hereto that **all of the Business** and all of Seller’s backlog, if any, relating to the Business **be transferred to Buyer.**” (§ 1.3(a)(i).)
- “Seller is engaged in the business of developing a line of software products currently known as Unix and UnixWare, the sale of binary and source code licenses to various versions of Unix and UnixWare, the support of such products and the sale of other products (‘Auxiliary Products’) which are directly related to Unix and UnixWare (collectively, the ‘Business’).” (Recital A.)
- “On the terms and subject to the conditions set forth in this Agreement, Seller will sell, convey, transfer, assign, and deliver to Buyer and Buyer will purchase and acquire from Seller on the Closing Date (as defined in Section 1.7), **all of Seller’s right, title and interest in and to the assets and properties of Seller relating to the Business** (collectively the ‘Assets’) identified on Schedule 1.1(a) hereto.” (§ 1.1(a).)
- “**All rights and ownership of UNIX and UnixWare**, including but not limited to all versions of UNIX and UnixWare and all copies of UNIX and UnixWare . . . including **source code**, source documentation, source listings and annotations . . . **such assets to include without limitation** . . . UNIX and UnixWare Source Code Products . . . Binary Product Releases . . . Products Under Development . . .” (Schedule 1.1(a) § I.)

“SVRX Licenses” Are Meant to Refer to “SVRX Royalties” in Product Supplements

- Section 4.16(a) describes the SVRX Royalties as “all royalties, fees and other amounts due under the SVRX Licenses (as listed in detail under item VI of Schedule 1.1(a) hereof and referred to herein as “SVRX Royalties).”
 - The only agreements “under” which “royalties, fee and other amounts” could be “due” were the Product Supplements. (1/17/07 Hatch Decl. Ex. 51 ¶¶ 10-14 (12/11/06 Maciaszek Decl.); Ex. 50 ¶¶ 13-17 (12/11/06 Broderick Decl.).)
 - Novell and Santa Cruz maintained such information by product, and after the closing, Santa Cruz reported that information to Novell by product. (Id.)
- APA defines Business as the development of “a line of software products currently known as UNIX and UnixWare, the sale of binary and source code licenses to various versions of UNIX and UnixWare, the support of such products and the sale” of “Auxiliary Products.”
 - The only agreements that licensed such versions and products were the corresponding Product Supplements. (Id.)
 - The only “source and binary licenses” that were for “sale” were the Product Supplements, which listed the fees and gave rise to a payment obligation. (Id.)
 - The Software and Sublicensing agreements did not identify any such fees or give rise to any payment obligation. (Id.)
- While the Software and Sublicensing Agreements may incorporate the Product Supplements, the Product Supplements do not incorporate the Software and Sublicensing Agreements and transform them into “SVRX Licenses.”

Novell's Interpretation Makes a Sham of the APA

- Section 1.1(a) grants to SCO “all right, title, and interest in and to the assets and properties of Seller relating to the Business.”
- Schedule 1.1(a) grants to SCO “All rights and ownership of UNIX and UnixWare including but not limited to” the “source code” to the “UNIX Source Code Products.”
- Schedule 1.1(a) grants SCO “All of Seller’s rights pertaining to UNIX and UnixWare under any software development contracts, licenses and any other contracts to which Seller is a party or by which it is bound and which pertain to the Business.”
- Schedule 1.1(a) grants SCO “All of Seller’s claims arising after the Closing Date against any parties to any right, property or asset included in the Business.”

Amendment No. 2 Makes Clear Novell's Rights Do Not Extend to Source Code

- B. Except as provided in Section C below, and notwithstanding the provisions of Article 4.16, Sections (b) and (c) of the Agreement, any potential transaction with an SVRX licensee which concerns a buy-out of any such licensee's royalty obligations shall be managed as follows:
1. Should either party become aware of any such potential transaction, it will immediately notify the other in writing.
 2. Any meetings and/or negotiations with the licensee will be attended by both parties, unless agreed otherwise. Novell's participation will be by personnel who are engaged in corporate business development.
 3. Any written proposal to be presented to the licensee, including drafts and final versions of any proposed amendments to the SVRX licenses, will be consented to by both parties prior to its delivery to the licensee, unless agreed otherwise.
 4. Prior to either parties' unilateral determination as to the suitability of any potential buy-out transaction, the parties will meet face to face and analyze the potential merits and disadvantages of the transaction. No such transaction will be concluded unless the execution copy of the amendment is consented to in writing by both parties, and either party will have the unilateral right to withhold its consent should it judge, for any reason whatsoever, the transaction to be contrary to its economic interests and/or its business plans and strategy.
 5. This Amendment does not give Novell the right to increase any SVRX licensee's rights to SVRX source code, nor does it give Novell the right to grant new SVRX source code licenses. In addition, Novell may not prevent SCO from exercising its rights with respect to SVRX source code in accordance with the Agreement.
 6. The parties agree that no member of Novell's sales force will receive a bonus, commission, quota attainment credit, or other type of sales incentive as a result of the buy-out of an SVRX license.
- C. Novell may execute a buy-out with a licensee without any approval or involvement of SCO, and will no longer be bound by any of the requirements stated in Section B. above, if: (i) SCO ceases to actively and aggressively market SCO's UNIX platforms; or (ii) upon a change of control of SCO as stated in schedule 6.3(g) of the Agreement.

Amendment No. 2 Makes Clear Novell's Rights Do Not Extend to Source Code

Novell ignores the second sentence of Paragraph B.5.

“In addition, Novell may not prevent SCO from exercising rights with respect to SVRX source code in accordance with the Agreement.”
(Amendment No. 2 § B.5)

- Paragraph B states “notwithstanding the provisions of Article 4.16, Sections (b) and (c),” making clear that B.5 limits Novell’s waiver rights.
- The second sentence of Paragraph B.5 does not exclude IBM, whose buyout was complete.
 - Buyouts discussed because no plausible basis existed for Novell to assert source code rights outside the buyout scenario.
 - If Novell could waive rights in advance or after a buyout, buyout limitation would be meaningless.

Novell Witnesses Agree With SCO's Position

Robert Frankenberg, Novell CEO at the time of APA:

Q. Do you have an understanding of what the purpose of 4.16(b) was?

A. Yes.

Q. Could you explain that purpose in your words?

A. This was to make sure that Novell continued to receive the SVRX license fees and that those efforts weren't interfered with.

Q. Was there any broader purpose than that?

A. No.

Q. Was it Novell's intent to maintain a veto on how SCO operated its business in the future except for protecting that royalty stream?

MR. JACOBS: Objection, lacks foundation, calls for speculation.

A. No.

Q. Other than actions by SCO which would interfere with that royalty stream, was Novell retaining the right to veto or waive any actions taken by SCO?

MR. JACOBS: Objection, lacks foundation, calls for speculation, the document speaks for itself, calls for a legal conclusion.

A. No.

Novell Witnesses Agree With SCO's Position

Ed Chatlos, Novell Chief Negotiator:

“Under the APA, Novell received shares of SCO common stock and other consideration, and retained rights to certain binary product royalty payments. SCO acquired all right, title, and interest in and to the UNIX and UnixWare business, operating system, and source code. In the transaction, it was my intent – and to my understanding was Novell’s intent – to sell the entire UNIX business to SCO, including source code and all associated copyrights.

* * * *

“Paragraph 4.16 of the APA was specifically designed and intended to protect Novell’s retained binary product royalty stream. **Based on the foregoing, including my understanding of the parties’ intent, I do not believe that Novell has any right to waive, or to direct or require SCO to waive, any of SCO’s source code rights, including under customer source code licenses.**”

Santa Cruz Witnesses Agree With SCO's Position

Doug Michels, Santa Cruz Founder and Senior Vice President at time of APA:

- Q. Continuing in paragraph 9 of your declaration on page 2, the last sentence of it reads: **There was no intent to grant Novell any right to waive or to direct or require SCO to waive, any of its intellectual property rights or protections contained in the UNIX licenses.** What's the basis for that statement?
- A. We bought the whole business.
- Q. Except for certain revenue streams though; isn't that right?
- A. We bought the whole business. We partially paid for it with the residual revenues from certain contracts.
- Q. As to those contracts, did Novell retain any rights?
- A. It was purely a financial arrangement. **We bought the whole business. The only rights they retained was rights preventing us from arbitrarily destroying that revenue stream.**

Novell's Conduct in the IBM Buyout Cannot Be Reconciled With Novell's Current Position

- April 1996: Novell unilaterally negotiates buyout of IBM royalties. (1/17/07 Hatch Decl. Ex. 17 (4/26/96 Buyout Agreement).) Santa Cruz objects to proposed IBM buyout, telling Mr. Frankenberg that “our agreements provide SCO with ownership and exclusive rights to license the UNIX source code.” (1/17/07 Hatch Decl. Ex. 25 (4/23/96 Letter from Mohan to Frank).)
- April-June, 1996: In letters to Santa Cruz, Mr. Frankenberg does not assert any 4.16(b) rights or dispute Santa Cruz's claim to “ownership and exclusive rights to license the UNIX source code.” (1/17/07 Hatch Decl. Exs. 22-27.)
- October 16, 1996: Novell and Santa Cruz sign Amendment X and Amendment No. 2 to APA.
- April-October 1996: Novell does not suggest at any time that it can simply exercise waiver rights under Section 4.16.

Novell's Admissions in the HP Buyout Contradict Novell's Current Position

“NOVELL retained or has acquired all rights to outstanding and future HP binary code royalty and license fee payments, but not source code royalties ('HP BINARY ROYALTY OBLIGATIONS'). NOVELL hereby warrants that as of NOVELL's signature date of this ADDENDUM, as provided below, **NOVELL has no present, or future, or reversionary interest in any such source code royalties.** NOVELL hereby warrants that NOVELL has full right and authority to modify the terms and conditions of the AGREEMENT with respect to the HP BINARY ROYALTY OBLIGATIONS. The purpose of this ADDENDUM is to simplify those obligations, as well as corresponding reporting obligations.”

– 1/28/00 Addendum To: HP's UNIX System Agreement (emphasis added).

Novell Understood It Was Out Of the UNIX and UnixWare Business After the APA

- On October 18, 1995, Larry Bouffard, Novell's Worldwide Sales Director for UNIX, wrote in an internal Novell document:

“We are obligated to give SCO all information, contracts, assets etc. pertaining to the UnixWare business and the old UNIX source code business. **They have bought it lock, stock and barrel. Once the transaction is closed (Nov.-Dec.) we will have no more involvement with this business.** Therefor [sic], if a contract is for UnixWare or UNIX, it will be SCO's.”

(5/18/07 James Decl. Ex. 93 (10/18/95 Bouffard e-mail) (emphasis added).)

- On November 8, 1995, Novell's Lou Ackerman proposed to Santa Cruz a Statement of Work for licensing and contract management permitting Novell to:

“**Act as SCO's worldwide agent for UnixWare (*) and SVRx** (and any other Novell source code products being transferred to SCO) licensing activities with OEM, Commercial, Government and Educational customers,” including “Responding to customer inquiries about the products and **transfer of ownership to SCO.**”

(5/18/07 James Decl. Ex. 94 at SCO1299982 (11/8/95 Ackerman e-mail).)

- On December 4, 1995, Novell Senior Product Manager Skip Jonas explained to other Novell members of transition team:

“As of the Closing Date (now set for 12/6), **all UNIX & UW agreements transfer to SCO Novell is out of the UNIX/UW business** after the Closing and does not have the right to sell UW.”

(5/18/07 James Decl. Ex. 92 (12/4/95 Jonas e-mail) (emphasis added).)

Under California Law, the Covenant of Good Faith and Fair Dealing Applies to Every Contract

“Every contract imposes upon each party a duty of good faith and fair dealing in its performance and its enforcement. This duty has been recognized in the majority of American jurisdictions, the Restatement, and the Uniform Commercial Code.”

- Carma Developers (Cal.), Inc. v. Marathon Dev. Cal., Inc., 2 Cal. 4th 342, 372 (1992) (citing authority).

Novell Does Not Even Argue that the Court Can Determine as a Matter of Law that Novell Waived SCO's Rights in Good Faith

Novell does not produce any evidence to dispute SCO's core claims on this point.

SCO's argument is and the evidence shows that Novell has exercised its purported rights of waiver in relation to SCO's claims against IBM:

- Without seeking to protect any binary royalty stream;
- After Novell and IBM formed their common-interest relationship;
- Where Novell has acquired the SuSE Linux business; and
- Where IBM has invested \$50 million in Novell.