

IN THE UNITED STATES BANKRUPTCY COURT  
FOR THE DISTRICT OF DELAWARE

In re: ) Chapter 11  
)  
The SCO GROUP, INC., et al.,<sup>1</sup> ) Case No. 07-11337 (KG)  
) (Jointly Administered)  
)  
Debtors. )

Hearing Date: September 16, 2008 at 10:00 a.m. prevailing Eastern time  
Objection Deadline: September 9, 2008 at 4:00 p.m. prevailing Eastern time

**DEBTORS' MOTION FOR (1) A DETERMINATION  
THAT STOCK OPTIONS GRANTED TO EXECUTIVES WERE  
AWARDED IN THE ORDINARY COURSE OF DEBTORS' BUSINESS AND (2)  
CONTINUING AUTHORITY TO GRANT ORDINARY COURSE STOCK OPTIONS**

The SCO Group, Inc. ("SCO") and SCO Operations, Inc. ("Operations") (SCO and Operations collectively, the "Debtors") seek a determining that stock options awarded to the Debtors' four executives pursuant to the Debtors' 2004 Omnibus Stock Incentive Plan on August 26, 2008 were awarded in the ordinary course of the Debtors' business, and for continuing authority to continue to grant similar awards thereafter. In support of this motion (the "Motion"), the Debtors respectfully state as follows:

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<sup>1</sup> The Debtors and the last four digits of each of the Debtors' federal tax identification numbers are as follows: (a) The SCO Group, Inc., a Delaware corporation, Fed. Tax Id. #2823; and (b) SCO Operations, Inc., a Delaware corporation, Fed. Tax ID. #7393.

## Jurisdiction

1. This Court has jurisdiction over these cases under 28 U.S.C. §§ 157 and 1334. This matter is a core proceeding per 28 U.S.C. § 157(b)(2) (A) and (M).

## Relevant Background<sup>2</sup>

### A. Ordinary Course Award of Stock Options

2. During the fiscal year ended October 31, 1998, SCO implemented the *1998 Stock Option Plan* (the “1998 Plan”) that provided for the granting of nonqualified stock options to purchase shares of common stock. On December 1, 1999, SCO’s board of directors approved the *1999 Omnibus Stock Incentive Plan* (the “1999 Plan”), which was intended to serve as the successor equity incentive program to the 1998 Plan. The 1999 Plan allowed for the grant of awards in the form of incentive and non-qualified stock options, stock appreciation rights, restricted shares, phantom stock and stock bonuses. Awards were granted to individuals in the Debtors’ employ or service.

3. On May 16, 2003 SCO’s stockholders approved the *2002 Omnibus Stock Incentive Plan* (the “2002 Plan”) upon the recommendation of the board of directors. The 2002 Plan permitted the award of stock options, stock appreciation rights, restricted stock, phantom stock rights, and stock bonuses. The exercise price of stock options must be equal to or greater than the fair market value of the common stock as of the date of grant.

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<sup>2</sup> For a detailed description of the Debtors’ background and operations, the Debtors respectfully refer the Court and parties in interest to the *Declaration of Darl C. McBride, Chief Executive Officer, in Support of First Day Pleadings* (Docket No. 3).

4. On April 20, 2004, SCO's stockholders approved the *2004 Omnibus Stock Incentive Plan* (the "2004 Plan") upon the recommendation of the board of directors. A copy of the 2004 Plan is attached hereto as Exhibit A. There have not been any plans since the 2004 Plan. Like the prior plans, the 2004 Plan is designed to promote the interests of SCO and its stockholders by incentivizing and rewarding employees who make a long-term contribution to the success of the company.

5. The 2004 Plan allows for the award of up to 1,500,000 shares of SCO's common stock and permits the award of stock options, stock appreciation rights, restricted stock, phantom stock rights, and stock bonuses. The 2004 Plan incorporates an evergreen formula pursuant to which on each November 1, the aggregate number of shares reserved for issuance under the 2004 Plan will increase by a number of shares equal to 3% of the outstanding shares on the day preceding (October 31). The 2004 Plan is administered by the Compensation Committee of SCO's board of directors (the "Committee").<sup>3</sup> The Committee has the ability to determine the terms of the option, the exercise price, the number of shares subject to each option, and the exercisability of the options. Stock options may have an exercise price equal to, less than, or greater than the fair market value of the common stock on the date of grant, except that the exercise price of incentive stock options must be equal to or greater than the fair market value of the common stock as of the date of grant. Shares issued pursuant to the 2004 Plan may be authorized and unissued shares, treasury shares or shares acquired by SCO for purposes of the 2004 Plan.

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<sup>3</sup> None of the Debtors' management team are on the Committee.

6. Under the terms of the 1998, 1999, 2002 and 2004 Plans, options generally expire 10 years from the date of grant or within 90 days of termination. Options granted under these plans generally vest at 25% after the completion of 1 year of service and then 1/36 per month for the remaining 3 years and would be fully vested at the end of 4 years.

7. SCO's board of directors may suspend, revise, terminate or amend any of the option plans at any time; provided, however, that stockholder approval must be obtained if and to the extent that the board deems it appropriate to satisfy Section 162(m) of the Code, Section 422 of the Code or the rules of any stock exchange on which the common stock is listed. No action under the option plans may, without the consent of the participant, reduce the participant's rights under any outstanding award.

8. There are various components to the 2004 Plan. The component of the 2004 Plan that is relevant for purposes of this Motion is the award of Options.<sup>4</sup> An Option is defined as "an option to purchase shares of Common Stock pursuant to Section 7 of the [Stock] Plan." 2004 Plan, § 2(s).

9. Pursuant to the 2004 Plan, the exercise price of an Option cannot be less than the Fair Market Value of the Common Stock on the date of the grant. 2004 Plan, § 7(b).

10. Pursuant to the 2004 Plan, the Options vest over a four year period following the grant and are exercisable as follows:

- 25% of Options on first anniversary of grant; and
- 1/36<sup>th</sup> per month thereafter.

2004 Plan, § 7(c).

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<sup>4</sup> Capitalized terms not otherwise defined have the meanings ascribed in the 2004 Plan.

11. As set forth above, SCO has implemented programs similar to the 2004 Plan since fiscal year 1998.

12. On August 26, 2008, the Committee approved the award of 580,000 shares of SCO's common stock to SCO's four executives (chief executive officer, chief operating officer, general counsel and chief financial officer). The award to the executives was at the exercise price of \$0.24 per Option, which was the trading price of the Common Stock as of the date of the grant.

13. The timing of the filing of SCO's bankruptcy petition coincided with the close of the company's fourth quarter and its fiscal year end. SCO and its Board were rightfully and understandably focused on ensuring that the filing had as minimal a disruption as possible to operations. Accordingly, the Committee did not consider or approve the award of Options for the Debtors' executives for fiscal year ending October 31, 2007 until August 26, 2008.

#### **Relief Requested**

14. The Debtors seek the entry of an order determining that stock options awarded to the Debtors' four executives pursuant their 2004 Omnibus Stock Incentive Plan on August 26, 2008 were awarded in the ordinary course of the Debtors' business, and seek continuing authority to continue to grant similar awards hereafter.

15. The Debtors have consulted with the Office of the United States Trustee ("UST") seeking its position on the Options subject of this Motion. The UST has indicated that it does not take a position. Accordingly, and in an abundance of caution, the Debtors file this Motion.

### Basis for Relief Requested

16. The Bankruptcy Code provides, in relevant part:

[T]he [debtor in possession] may enter into transactions ... in the ordinary course of business, without notice or a hearing, and may use property of the estate in the ordinary course of business, without notice or hearing.

11 U.S.C. § 363(c)(1). Further, “the [debtor in possession] may operate the debtor’s business” unless otherwise ordered by the Court. 11 U.S.C. § 1108.

17. On the other hand, transactions outside the ordinary course of business are subject of notice, hearing and court approval. *See* 11 U.S.C. § 363(b).

18. “Although the determination of whether a transaction is in the ordinary course of business can have broad implications, ‘[n]either the Bankruptcy Code nor its legislative history provides a framework for analyzing whether particular transactions are in the ordinary course of a debtor’s business.’” *In re Nellson Nutraceutical, Inc.*, 369 B.R. 787, 797 (Bankr. D. Del. 2007) (quoting *In re Roth American, Inc.*, 975 F.2d 949, 952 (3d Cir. 1992)).

19. “In order to determine whether or not a transaction falls in the ordinary course of business most courts, including the Third Circuit, have adopted a two-step inquiry.” *Id.* “This inquiry consists of looking at the transaction from horizontal and vertical dimensions.” *Id.* “The test for the horizontal dimension ‘is whether, from an industry-wide perspective, the transaction is of the sort commonly undertaken by companies in that industry.’” *Id.* (quoting *Roth American*, 975 F.2d at 953). The vertical dimension “analyzes the transactions from the vantage point of a hypothetical creditor and the inquiry is whether the transaction subjects a creditor to economic risk of a nature different from those he accepted when he decided to extend

credit.” *Id.* (quoting *Roth American*, 975 F.2d at 953). Pursuant to the vertical test, “a debtor’s pre-petition business practices and conduct is the primary focus of the vertical analysis.” *Id.* “The Court must ‘also consider the changing circumstances inherent in the hypothetical creditor’s expectations.’” *Id.*

20. The Debtors submit that the horizontal and vertical dimensions are met. The Options subject of the 2004 Plan are common in the Debtors’ industry, evidence of which will be proffered at the hearing on this Motion. With respect to the so-called “vertical test”, the evidence will show that SCO had the 2004 Plan, and others like it since at least fiscal year 1998, a fact that is well-known through the filings required of public companies, so hypothetical creditors would be well aware of the “risk” inherent in the Incentive Program. The Debtors further submit that the award of Options under the 2004 Plan does not harm or have any negative impact on creditors since an Option simply allows an employee to purchase shares of SCO and does not deplete the Debtors’ cash or diminish the value of their other assets in any fashion.

21. Accordingly, the Debtors submit that the Options awarded to the Debtors’ four executive employees on August 26, 2008 were made in the ordinary course of business.

#### **Notice**

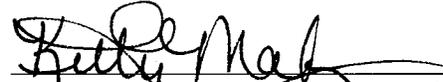
22. Notice of this Motion has been or will be given to the following parties or, in lieu thereof, to their counsel, if known: (i) the Office of the United States Trustee; (ii) the creditors holding the 20 largest unsecured claims against the Debtors’ estates (on a consolidated basis); and (iii) any party which has filed a request for notices with this Court prior to the date of

this Motion. The Debtors submit that, in light of the nature of the relief requested, no other or further notice need be given.

WHEREFORE, the Debtors respectfully request that the Court enter an order determining that stock options awarded to the Debtors' four executives pursuant their 2004 Omnibus Stock Incentive Plan on August 26, 2008 were awarded in the ordinary course of the Debtors' business, authorizing the Debtors to continue to make ordinary course awards of Options and granting such other and further relief as is just and proper.

Dated: August 27, 2008

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