

**UNITED STATES BANKRUPTCY COURT  
FOR THE DISTRICT OF DELAWARE**

In re: )  
 ) Chapter 11  
The SCO Group, Inc., et al., )  
 ) Case No. 07-11337 (KG)  
Debtors. ) (Jointly Administered)

**Objection Deadline: November 13, 2008 at 4:00 p.m. (prevailing Eastern time)**  
**Hearing: November 20, 2008 at 9:30 a.m. (prevailing Eastern time)**

**NOVELL'S MOTION FOR ENTRY OF ORDER CONFIRMING CONSTRUCTIVE TRUST AND DIRECTING THE DEBTORS TO PAY FUNDS TO NOVELL**

Novell, Inc. hereby moves the Court to (i) confirm the parties' agreement on the amount of funds that debtors and debtors in possession The SCO Group, Inc., and SCO Operations, Inc. (together, "SCO") hold in trust for Novell and (ii) order SCO to pay those funds to Novell now.

**I. PRELIMINARY STATEMENT**

1. In granting Novell stay relief last November to liquidate its claims against SCO in United States District Court for the District of Utah (the "District Court"), this Court reserved certain issues arising from Novell's claim to a constructive trust. The Court's rationale was that these issues affected whether certain funds were property of the SCO bankruptcy estates under Bankruptcy Code section 541, a subject the Court noted is squarely within the Court's core jurisdiction.

2. In April and May of this year, the District Court conducted a bench trial, issuing an opinion in July. The parties subsequently met and conferred and have agreed that, in light of the District Court's orders and the application of agreed-upon principles of trust tracing, it is appropriate to establish a trust in Novell's favor in the amount of \$625,486.90. Novell therefore seeks confirmation of that agreement by this Court and the imposition of a constructive trust in that amount.

3. Though the parties have agreed on the appropriate amount of a constructive trust, they disagree on when to transfer possession of the trust funds to Novell. Novell requests payment now; SCO wants payment suspended until some future date, after appeals of the District Court's orders have been resolved. Novell submits that because the money in question belongs (and has always belonged) to Novell, not SCO, payment now is appropriate, a step, moreover, that also will not harm SCO.

## **II. BACKGROUND**

### **A. Prepetition Events**

4. Before filing these chapter 11 cases, SCO was involved in litigation against various parties, including Novell, involving SCO's claims that the other parties were interfering with SCO's alleged ownership of certain software copyrights. (*See* Memorandum Opinion (filed herein November 27, 2007) (the "Opinion") 1-2.)

5. On August 10, 2007, Novell won important rulings against SCO on summary judgment in the District Court. (Opinion 3-4.) That left only Novell's counterclaims against SCO to try. (Opinion 4.) The District Court held that a constructive trust "was an appropriate remedy" but could not quantify the amount of the trust based on the summary judgment record and left that quantification for later determination. (Affidavit of Greg Jones [etc.] (filed October 4, 2008, Docket No. 91, Ex. B (District Court Opinion) at 98 ("Although the court finds that Novell meets the requirements for the imposition of a constructive trust, the question of fact as to the SVRX portion of the 2003 Sun and Microsoft Agreements precludes the court from imposing a trust for the appropriate amounts.").)

6. The trial on the residual issues left by the summary judgment was set for September 14, 2007, a Monday. (Opinion 4.) Having all but lost its litigation with Novell, the Debtors filed their voluntary chapter 11 petitions before this Court on September 11, 2007, the preceding Friday. The filing stayed the District Court litigation.

**B. Partial Stay Relief for Novell and Issues Reserved by this Court**

7. On October 4, 2007, Novell moved for stay relief to try the remaining issues in the District Court litigation. SCO opposed Novell's request. (*See* Novell, Inc.'s Motion for Relief from Automatic Stay [etc.] (filed October 4, 2007) (Docket No. 89) (the "Novell Stay Motion"); Debtors' Memorandum of Law in Response to Novell, Inc.'s Motion for Relief From Automatic Stay [etc.] (filed October 23, 2007) (Docket No. 150).) The Court granted the Novell Stay Motion, but reserved for itself issues concerning the imposition of a constructive trust. (Opinion 9-10; Order Granting Novell's Motion for Relief from the Automatic Stay to Proceed with the Lawsuit (filed November 27, 2007; Docket No. 233) (the "Stay Relief Order").)

**C. The District Court Trial, Ruling, and Aftermath**

8. With the stay lifted, the District Court trial occurred in late April - early May, 2008. On July 16, 2008, the District Court issued its Findings of Fact, Conclusions of Law, and Order ("Trial Order"). (Declaration of David E. Melaugh in Support of Novell's Motion for Entry of Order Confirming Constructive Trust and Directing the Debtors to Pay Funds to Novell (Melaugh Decl.), ¶ 4, Ex. A.) In its Trial Order, the District Court found that:

- SCO owes Novell a fiduciary duty to collect, account for, hold in trust, and remit to Novell all "SVRX Royalties." (Trial Order at 5.)
- SCO entered into a license with Sun Microsystems in February 2003, pursuant to which SCO collected royalties. (*Id.* at 17.)
- \$2,547,817 of the Sun royalties SCO collected were SVRX Royalties. (*Id.* at 42.)
- SCO's failure to account for and remit those SVRX Royalties was a breach of its fiduciary duties to Novell, a conversion, and an unjust enrichment. (*Id.* at 37-39.)

9. In the wake of the Trial Order, the parties reached an agreement that, based on an uncontested reading of trust tracing law and SCO's relevant daily balance information, the appropriate amount of a constructive trust is \$625,486.90 ("Trust Funds"). (Melaugh Decl., ¶ 5.) SCO subsequently reported this agreement in July 2008 quarterly securities filings. (Declaration

of Adam A. Lewis in Support of Novell's Motion for Entry of Order Confirming Constructive Trust and Directing the Debtors to Pay Funds to Novell, ¶ 4, Ex. A (excerpts from SCO's July 31, 2008 Form 10-Q).)

10. The parties could not agree, however, on whether the Court now should order transfer of possession of the Trust Funds to Novell. (Melaugh Decl., ¶ 6.) SCO wants to postpone payment of the Trust Funds, while Novell believes they should be paid without further delay. (*Id.*)

### **III. RELIEF REQUESTED**

11. Novell now asks the Court to (i) confirm the parties' agreement regarding the amount of the Trust Funds and (ii) order SCO to pay the Trust Funds to Novell forthwith since they are Novell's property, not SCO's, property that SCO has no legitimate claim to use .

### **IV. THIS COURT'S ORDER REGARDING THE TRUST FUNDS WILL BE A FINAL ORDER READY FOR ENFORCEMENT**

12. There appears to be no dispute that this Court should enter an order imposing a constructive trust in the amount of \$625,486.90. Such an order will be a final order leaving nothing further for this Court to decide. With nothing left for the Court to determine on the constructive trust, there is no procedural reason why the Court should not also order SCO to transfer the Trust Funds to Novell.

#### **A. Bankruptcy Court Jurisdiction Over What Is Estate Property**

13. Code section 541(a) creates a bankruptcy estate consisting of the debtor's prepetition property interests of all kinds. However, under Code section 541(d), the estate does not include property held in trust for another, including property held in constructive trust. *E.g., In re Flanagan*, 503 F.3d 170, 180-82 (2d Cir. 2007); *In re Coupon Clearing Service, Inc.*, 113 F.3d 1091, 1099 (9th Cir. 1997).

14. Whether property is estate property is a matter committed to the bankruptcy court to decide and on which the bankruptcy court may issue a final order. *See* 28 U.S.C. §§ 157(a) (permitting district courts to refer bankruptcy jurisdiction to bankruptcy courts); 28 U.S.C. §§

157 (b)(1) (permitting bankruptcy courts to “hear and determine . . . core proceedings”), (b)(2)(A) (including in core matters proceedings concerning “administration of the estate”); 28 U.S.C. § 1334(e)(1) (bankruptcy court has exclusive jurisdiction over all estate property); *Pension Benefit Guar. Corp. v. Continental Airlines, Inc. (In re Continental Airlines, Inc.)*, 138 B.R. 442, 445 (Bankr. D. Del. 1992); *Verit Hotel & Leisure (Int’l) Ltd. v. Carway*, 240 B.R. 771, 775 (D. Az. 1999) (affirming bankruptcy court’s determination that bankruptcy trustee held constructive trust over stock held by foreign corporation, stock being part of bankruptcy estate).

15. The bankruptcy court’s determination regarding whether there is a constructive trust held by a debtor in favor of a third party is a proceeding regarding whether the property is estate property. See *In re Flanagan*, 503 F.3d at 181-82; *In re Coupon Clearing Serv., Inc.*, 113 F.3d 1091 at 1099 (9th Cir. 1997). The question of whether a debtor holds property in trust for another is one of state law, with the estate having no greater rights than the debtor had prepetition. *In re Coupon Clearing Service, Inc.*, 113 F.3d 1091, 1099 (9th Cir. 1997). A constructive trust need not have been judicially determined prepetition to exist in order for the trust corpus to be excluded from the estate, nor does the Code’s policy of ratable distribution to creditors trump a particular party’s rights under a constructive trust. *Mullins v. Burtch (In re Paul J. Paradise & Assoc., Inc.)*, 249 B.R. 360, 370-71 (D. Del. 2000).

**B. An Order Confirming the Constructive Trust Agreement Will Be A Final Order Leaving the Court Nothing Further to Determine Before Enforcement**

16. A bankruptcy court order is a final, appealable order under 28 U.S.C. section 158(a)(1) if it resolves a discrete issue between the parties, leaving only for the Court to execute the judgment it has just rendered. *Camacho v. Doral Fin. Corp. (In re Camacho)*, 361 B.R. 294, 298-99 (B.A. P. 1st Cir. 2007); *B-Line, LLC v. Kirkland (In re Kirkland)*, 379 B.R. 341, 343 (B.A.P. 10th Cir. 2007) (nothing left for court to do but execute judgment); see also, e.g., *Rivera v. Miranda*, 376 B.R. 382, 384-85 (D.P.R. 2007) (resolution of discrete issue). A ruling by the bankruptcy court finding or denying the existence of a constructive trust that ends a dispute is a final order. See, e.g., *In re Coupon Clearing Serv., Inc.*, 113 F.3d at 1098-99 (appeal of

summary judgment finding whether proceeds of coupons were property of estate to which lien could attach or subject to constructive trust); *Mullins v. Burtch, supra* (court determines trustee's strong-arm power applying state law rights of bona fide purchaser superior to constructive trust).

17. That is the case here. There is a discrete matter before this Court as a result of the Court's Stay Relief Order: determination of the balance of the constructive trust issue. If the Court approves the parties' constructive trust agreement, there is nothing further for this Court to do to decide the constructive trust issue. Rather, all that is left is for the parties to abide by the Court's judgment.

18. That being so, there is no reason for the Court to postpone transfer of the Trust Funds to Novell. Indeed, there is additional reason for the inclusion of that remedy in the Court's order. Although the bankruptcy courts have jurisdiction over SCO, jurisdiction to determine what is estate property and exclusive jurisdiction over estate property, they have no jurisdiction over property that is not property of the estate. *E.g., Rutherford Hosp. v. RNH Pshp.*, 168 F.3d 693, 699 (4th Cir. 1999) ("a bankruptcy court's jurisdiction does not extend to property that is not part of a debtor's estate"); *In re McClellan*, 99 F.3d 1420, 1422 (7th Cir. 1996) ("Bankruptcy courts do not have subject matter jurisdiction and cannot administer property excluded from or outside the bankruptcy estate."). Since under Code section 541(d) the Trust Funds are not estate property over which the Court has jurisdiction, there are no grounds for the Court to permit SCO to retain those funds a moment longer under the aegis of the Court's protective jurisdiction.

19. Not only does SCO lack any claim to the Trust Funds or their use, but also it will suffer no harm if ordered to pay the them to Novell now. It cannot use the funds in the meantime – it holds them in trust for Novell.<sup>1</sup> Nor is there any indication that SCO would be unable to recover the Trust Funds from Novell some time hence should SCO succeed in having the underlying rulings by the District Court overturned on appeal. There is therefore no reason for

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<sup>1</sup> And how would SCO replace the Trust Funds if it did spend them given its limited present and prospective resources?

SCO to retain possession of the Trust Funds other than to deny them to Novell. That kind of punitive intransigence is no reason for a court of equity to deny a rightful owner its property.<sup>2</sup>

20. SCO may argue that Novell should have brought this motion as a complaint to commence an adversary proceeding under Fed. R. Bankr. P. 7001(a). However, even the full scope of the issues this Court reserved to itself would not have to be brought under Rule 7001(a). Rather, following the District Court's decisions, the remaining issues would have been far narrower than the full panoply of issues a typical Rule 7001(a) proceeding to recover money or property ordinarily would entail. Indeed, the reality is that this motion is an offshoot of litigation in the District Court that would have been an adversary proceeding if initially brought in this Court. There is no purpose in requiring this narrow residual aspect of the litigation be converted into an adversary proceeding when the issues eventuating in it arose and were decided in the context of the District Court equivalent of an adversary proceeding. Providing both parties the procedural benefits and protections that the adversary proceeding requirement was designed to foster serves no purpose in the present circumstances. Indeed, this motion is, in essence, the analogue of a motion in a pending adversary proceeding.

21. Accordingly, if the Court approves the Constructive Trust Agreement, it should also order SCO to transfer the Trust Funds to Novell's rightful possession without delay.

## V. CONCLUSION

This Court expressly reserved issues concerning the imposition of a constructive trust as coming within its jurisdiction. On those issues, the Court is empowered to make a binding final determination. Subject to the Court's approval, the parties have reached an agreement regarding


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<sup>2</sup> Even if SCO somehow could have made a theoretical case for being able to use the Trust Funds pending further proceedings with Novell, it cannot make a convincing argument for doing so in the present circumstances. Having recently stipulated to stay relief to allow the IPO Plaintiffs to prosecute their claims against SCO (*see* Motion for Approval of Stipulation for Relief from Automatic Stay with Respect to IPO Plaintiffs), SCO has voluntarily agreed to begin absorbing the cost of defending itself in that litigation. If SCO has money enough to agree to begin paying its legal fees in that case, then paying Novell the Trust Funds will not compromise its financial condition, either.

the funds SCO holds in trust in light of the District Court's rulings. Novell asks the Court to confirm the parties' trust fund agreement and order SCO to pay the Trust Funds to Novell.

Dated: October 29, 2008  
Wilmington, Delaware

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