

IN THE UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF DELAWARE

In re:)	Chapter 11
)	
The SCO GROUP, INC., <u>et al.</u> , ¹)	Case No. 07-11337 (KG)
)	(Jointly Administered)
)	
Debtors.)	Related Docket No. 278 and 288

**RESPONSE TO NOVELL’S OBJECTION TO DEBTORS’ MOTION TO APPROVE
THE ASSUMPTION OF NONRESIDENTIAL REAL PROPERTY LEASES**

The SCO Group, Inc. (“SCO Group”) and SCO Operations, Inc. (collectively, the “Debtors”), respond to the *Objection of Novell, Inc. to Motion to Approve the Assumption of Nonresidential Real Property Leases with GRE Mountain Heights Property LLC and Canopy Properties, Inc.* (Docket No. 288) (the “Objection”) as follows:

1. The Debtors filed the *Motion of the Debtors to Approve the Assumption of Nonresidential Real Property Leases with GRE Mountain Heights Property LLC and Canopy Properties, Inc.* (Docket No. 278) (the “Motion”)² seeking approval of their business decision to extend their New Jersey and Utah Leases, and in so doing, reduce the space rented and the monthly rent required for such facilities – typically a noncontroversial matter that does not require an inordinate expenditure of administrative expense to defend, especially where reduction in administrative expense to the estate is the issue raised.

¹ 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.

² Capitalized terms not otherwise defined have the meaning ascribed in the Motion.

2. However, Novell, Inc. questions the Debtors' business judgment, arguing that: (i) the Debtors' estates will be burdened with the financial commitment of the NJ Lease for an additional three years; (ii) the NJ Lease transaction is arguably a new lease rather than an assumption of a modified lease; (iii) the Debtors' Motion fails to explain the genesis and rationale for their decision; and (iv) no information has been provided with respect to the Utah Lease.

3. As a preliminary matter, if the leases are really "new" leases rather than assumption of existing leases, then the Debtors do not need the relief they are seeking, since, as debtors in possession, they can continue to operate their business, including to negotiate terms of ordinary course contracts and leases, such as leases of nonresidential real property, without the need for court approval. 11 U.S.C. § 363. However, since the documents *amend* certain of the terms of the current leases, the Debtors thought it appropriate to seek approval under 11 U.S.C. § 365.

4. Despite the Debtors' representations that the leases, as amended, will reduce space and reduce rent, thereby *reducing* the administrative expenses of the estates, Novell argues that the Debtors have failed to satisfy their burden of proof. First, the Debtors submit that those representations are sufficient to satisfy the business judgment test for purposes of the Motion. Second, there is no requirement that a motion contain evidence; a motion is simply a request for relief. A motion for court approval of the assumption of an unexpired lease is governed by Rules 6006 and 9014 of the Federal Rules of Bankruptcy Procedure. The Rules require that a motion state with particularity the grounds therefor. *See* Fed.R.Bankr.P. 6006, 9014. The Debtors submit that sufficient grounds have been pled. The point of notice procedures is to give creditors and parties in interest an opportunity to review and object to the relief sought. The Debtors will

demonstrate at the January 8, 2008 hearing that in addition to the bases pled in the Motion, other sound business reasons support the assumption of the amended leases.

5. Novell further complains that the Debtors have broken even on their operations on a cash flow basis, despite the fact that the proposed leases would reduce their monthly operating expenses. Novell is a competitor of the Debtors and a party with whom the Debtors are litigating against.

6. As described in the Motion, the leases comprise the Debtors' office space for their corporate headquarters and houses the majority of its non-telecommuting employees, including their accounting and finance departments, the corporate officers, marketing and human resources, engineers and account managers.

7. Over the years preceding the filing of these cases, and in the ordinary course of their business, the Debtors have amended their leases to suit their needs.

8. Prior to the Petition Date, and as disclosed in its public filings, as well as the *Declaration of Darl C. McBride, Chief Executive Officer in Support of First Day Pleadings* ("McBride Declaration") (Docket No. 3), sales of SCO's UNIX-based products and services, historically its primary source of revenue, have declined over the last several years. Such decline has resulted in, among other things, periodic reduction in the number of the Debtors' employees.

9. Since the Petition Date, SCO Group has negotiated with both landlords to amend the leases to, among other things, extend the terms thereof, reduce space and reduce the monthly rent. As set forth in the Motion, the NJ Lease was amended as follows:

a. For the months of January, February and March 2008, the Debtors shall continue to pay the "Fixed Rent" it is currently paying under the original lease in the amount of Forty Four Thousand One Hundred Sixty Seven and 50/100 Dollars (\$44,167.50).

b. During such three (3) month period, \$9,430.69 per month (\$28,292.07) will be held by Landlord as an additional Security Deposit in accordance with the terms and provisions of the Lease.³

c. Beginning on April 1, 2008, the Fixed Rent payable by the Debtors shall be Three Hundred Eighteen Thousand Seven Hundred Ten and 88/100 Dollars (\$318,710.88) per annum (exclusive of tenant electricity), payable in monthly installments of Twenty Six Thousand Five Hundred Fifty Nine and 24/100 Dollars (\$26,559.24).

d. The term of the NJ Lease is extended through December 31, 2010.

e. The space rented by the Debtors shall be reduced from 21,983 square feet to 11,183 square feet.

10. A copy of the amendment to the Utah Lease is attached as Exhibit A. In sum, the

Utah Lease was amended as follows:

a. Utah Lease is extended for period of one year commencing January 1, 2008 (the "Effective Date").

b. Upon the Effective Date, the Debtor surrenders to Utah Landlord approximately 9,738 Rentable Square Feet, bringing total rented premise to approximately 11,480 Rentable Square Feet.

c. Upon the Effective Date, the annual Base Rent shall be \$252,560.00 down from \$524,883.00.

d. Upon the Effective Date the Debtor's percentage share of the operating cost shall be reduced from 53.05% down to 30.6%.

e. If Debtor fails to make any payment required under the Utah Lease in excess of \$1,000 within ten (10) business days of receiving written notice from Landlord, the failure to make such payment will constitute an Event of Default and give Landlord the right to terminate the Utah Lease upon thirty (30) days' written notice.

³ Novell is quick to point out that the rent for three months will remain the same under the NJ Lease. However, ignores the fact that \$28,292.07, or \$9,430.69 per month, is to be held as an additional Security Deposit. Therefore, while the rent amount is technically the same, in practical terms, the rent was reduced by \$9,430.69 for that period of time.

Assumption Of Leases

11. The Debtors and Novell agree that the decision whether the court should approve the trustee's decision to assume an executory contract depends on the trustee's exercise of its "business judgment." *See e.g., NLRB v. Bildisco & Bildisco*, 465 U.S. 513, 523 (1984) ("traditional 'business judgment' standard applied by the courts to authorize rejection of [] ordinary course executory contract."). *See also*, Objection, ¶ 8.

12. "Generally, a court will give great deference to a debtor's decision to assume or reject an executory contract. A debtor need only show that its decision to assume or reject the contract is an exercise of sound business judgment – a standard which we have concluded many times is not difficult to meet [citations omitted]. We will not substitute our own business judgment for that of the Debtor, nor will we disturb its decision to reject the [contract] unless the 'decision is so unreasonable that it could not be based on sound business judgment, but only on bad faith or whim.' *In re III Enterprises Inc. V*, 163 B.R. 453, 469 (Bankr. E.D. Pa. 1994) (citations omitted). *See also, In re Crystalin, LLC*, 293 B.R. 455, 463 – 64 (8th Cir. BAP 2003) ("[The business judgment test] is not an onerous one ...").

13. "[I]n reviewing a trustee's or debtor-in-possession's decision to assume an executory contract [] a bankruptcy court sits as an overseer of the wisdom with which the bankruptcy estate's property is being managed by the trustee or debtor-in-possession, and not, as it does in other circumstances, as the arbiter of disputes between creditors and the estate ..."
Crystalin, 293 B.R. at 464. "Where the trustee's request is not manifestly unreasonable or made in bad faith, the court should normally grant approval 'as long as [the proposed action] *appears* to enhance [the] debtor's estate ...[and] the bankruptcy court should not interfere with the trustee

or debtor-in-possession's business judgment 'except upon a finding of bad faith or gross abuse of their "business discretion."'). *Id.* (emphasis in original).

14. Here, the Debtors have amply stated sound business judgment in negotiating amendments to the leases that should not be second guessed by the Court as suggested by Novell. The amendments reduce the space and the corresponding monthly rent, but allows the Debtors sufficient space to continue its operations efficiently. Further, there are no cure amounts due to either of the landlords. Accordingly, the result of the assumption will be to reduce the Debtors' ongoing administrative expenses.

15. The cases cited by Novell are inapposite. In *In re Global Int'l Airways*, the court denied approval of the assumption of a lease of an airplane because the debtor would have to spend between \$1.9 million and \$2.9 million over a three month period of time to cure the defaults and the debtor's projections failed to consider foreseeable contingencies. 35 B.R. 881, 887 - 88 (Bankr. W.D. Mo. 1983). Likewise, in *In re Angelo Entergy Ltd.*, the debtor proposed to assume employment contracts that would *increase* its operating expenses; especially since the debtor had previously obtained approval of an employee stock option plan that was an integral part of the employees' compensation. 41 B.R. 337, 340 - 41 (Bankr. S.D.N.Y. 1984). In *Crystalin*, the debtor sought approval of the assumption of an unexpired lease because it thought it would lead to a sale and quick end to the debtor's case. *Crystalin*, 293 B.R. at 464 -65. The only issue before the bankruptcy court was "whether assumption was likely to benefit the estate." *Id.* at 464. The bankruptcy court denied the relief, but made a finding that no default existed. *Id.* at 465. The Bankruptcy Appellate Panel reversed the denial of the relief, affirming the debtor's business judgment, finding that the bankruptcy court abused its discretion in not granting the motion for relief from the order disapproving the assumption. *Id.*

16. Accordingly, the Debtors submit that the assumption of the leases should be approved and the Objection overruled.

Notice

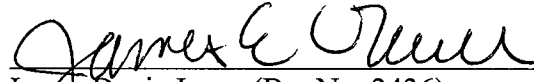
17. Notice of this response will be provided by hand delivery, or facsimile, or overnight mail, or electronic mail to: (1) the Office of the United States trustee for the District of Delaware; (2) NJ Landlord at GRE Mountain Heights Property, LLC c/o Vision Equities, LLC, 49 Old Bloomfield Avenue, Mountain Lakes, New Jersey 07046; (3) Utah Landlord; and (4) all parties who have timely filed requests for Notice under Bankruptcy Rule 2002.

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WHEREFORE, the Debtors respectfully request entry of an order granting the Motion and overruling the Objection, as well as granting any other and further relief the Court deems just and proper.

Dated: January 4, 2008

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