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IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF UTAH

THE SCO GROUP, INC., a Delaware corporation, Plaintiff/Counterclaim-Defendant, vs. NOVELL, INC., a Delaware corporation, Defendant/Counterclaim-Plaintiff.	**REPLY MEMORANDUM IN SUPPORT OF SCO'S MOTION FOR JUDGMENT ON THE PLEADINGS ON NOVELL'S CLAIMS FOR MONEY OR CLAIM FOR DECLARATORY RELIEF** Civil No. 2:04 CV-00139 Judge Dale A. Kimball Magistrate Brooke C. Wells

Plaintiff/Counterclaim-Defendant, The SCO Group, Inc. ("SCO"), respectfully submits this Reply Memorandum in Support of its Motion for Judgment on the Pleadings on Novell's Claims for Money or Claim for Declaratory Relief.

PRELIMINARY STATEMENT

Novell's opposition reflects a misapprehension of, or desire not to confront, the basic law of agency. Novell's claims for money concern this question: Is Novell entitled to money? Novell alleges that SCO acted as Novell's agent in signing the SCOsource Agreements and that SCO lacked the authority to do so. Under those facts and the well-established law, Novell could be entitled to the payments under the Agreements only if it had ratified them – which Novell now emphasizes it has not done. SCO therefore brings this Motion, because Novell fails to allege facts necessary for Novell to win its claims for money, and the Court cannot even infer "the opposite" of what Novell has alleged.

Novell improperly seeks to avoid what the Tenth Circuit has long recognized as "the horns of a dilemma," contending that "as between" itself and SCO, it should have the money it seeks. Under the law, however, whether the agent holds the money paid for its allegedly unauthorized contract has nothing to do with the merits of the principal's claim for the money: "It is repugnant in every sense of justice and fair dealing that a principal shall avail himself of the benefits of an agent's act and at the same time repudiate his authority." Yahola Sand & Gravel Co. v. Marx, 358 P.2d 366, 372 (Okla. 1960) (citing authority, quotations omitted). The most recent authority confirms: "Once the principal has ratified the agent's act, the agent is subject to a fiduciary duty to account to the principal as if the agent had acted with actual authority," where

"legal relations as between agent and principal are affected by whether the agent has acted with actual authority." Restatement (Third) of Agency § 4.02, Comment b (2006) (emphasis added).

It is also true that under its allegations, whether it is a principal or not, Novell has rendered the Agreements "void" – legal nullities for which Novell has no entitlement to the payments made thereunder. In short, on SCO's Motion, the only question is whether Novell has any right to payments under either unratified or void contracts. It does not.

ARGUMENT

I. NOVELL CANNOT PREVAIL ON ITS CLAIMS FOR MONEY.

Novell mistakenly argues (at 2-5) that SCO must prove "that an agent acting in excess of its authority is entitled to keep the proceeds of that excess." Like any plaintiff seeking to recover money from a defendant, Novell must allege facts giving it the right to the money at issue. Novell has failed to make such allegations.

A. The Basic Law of Agency.

Contending as its central argument (at 1) that "[r]atification is a matter between Novell and the licensee," Novell misapprehends the law of agency. In disavowing them, Novell made the decision that the SCOsource Agreements do not fall under the principal-agent relationship between itself and SCO. It makes sense that an alleged principal cannot have the fruits of such a contract. The most recent authority confirms:

> Ratification has an immediate effect on legal relations between the principal and agent . . . . Ratification recasts those legal relations as they would have been had the agent acted with actual authority. Legal consequences thus "relate back" to the time the agent acted. . . . Once the principal has ratified the agent's act, the agent is subject to a fiduciary duty to account to the principal as if the agent had acted with actual authority.
> . . . .

> [L]egal relations as between agent and principal are affected by whether the agent has acted with actual authority . . . . The effect of actual authority, which the ratification provides, relates to an action that the agent has already taken.

Restatement (Third) of Agency § 4.02, Comment b (2006) (emphasis added). "That is, when a person ratifies another's act, the legal consequence is that the person's legal relations are affected as they would have been had the actor been an agent acting with actual authority at the time of the act." Id. § 4.01, Comment b.[1]

The longstanding authority – including precedent cited in SCO's opening memorandum which Novell declines to address – emphasizes the inequity of the position Novell here seeks to maintain. "A principal may not, in equity, ratify those parts of the transaction which are beneficial and disavow those which are detrimental." The N. River Ins. Co. v. Transamerica Occidental Life Ins. Co., No. Civ. A. 399-CV-0682-L, 2002 WL 1315786, at *7 (N.D. Tex. June 12, 2002) (Ex. A) (citations and quotations omitted). "It is repugnant in every sense of justice and fair dealing that a principal shall avail himself of the benefits of an agent's act and at the same time repudiate his authority." Yahola Sand & Gravel Co. v. Marx, 358 P.2d 366, 372 (Okla. 1960) (citing authority, quotations omitted). Seeking to preserve some later argument that counterparties like Microsoft and Sun do not have any rights under their 2003 agreements with SCO, Novell plainly cannot recover any alleged "SVRX Royalties" under those agreements.

[1] The same rules apply even as to someone who was only purporting to be an agent of the principal – a situation in which, by Novell's logic, the principal supposedly would be even more "entitled" to any benefits the purported agent had received. Instead, the law provides that "if he was not an agent when he acted, the subsequent ratification by the principal subjects him to the liability of a fiduciary with respect to the transaction. Thus, if he made a profit or received property which would have been a violation of his fiduciary duty if in fact he had been an agent, the ratification subjects him to a duty to pay to the principal what he has received." Id. § 4.08, Comment a.

These equitable principles alone make clear that permitting Novell to recover any alleged SVRX Royalties would result in a "manifest injustice" warranting reconsideration of the Court's Order dated August 10, 2007. (SCO's Opening Mem. at 2.)

B. Novell's Argument About SCO's Supposed Burden Is Mistaken.

Novell therefore misses the point in maintaining (at 3-4) that the four cases cited in SCO's opening brief on which Novell chooses to focus do not hold that "where an agent improperly takes money from third parties in the principal's name, the *agent* is entitled to keep that money if the principal disclaims the agent's authority." The cases do not need to show that for SCO to prevail on its Motion; they need only show, as they do, that the principal cannot have the fruits of a contract that an agent negotiated and that the principal has disavowed. (SCO's Opening Mem. at 7-8.)

The precedent makes clear that the principal's lack of entitlement to the money paid under such a contract does not turn on who has possession of the money. The commentary to Section 47 of the Restatement (First) of Restitution, which SCO cited and which Novell does not dispute as relevant authority, provides the following, telling illustrations:

> 1. A shows B a telegram from C, A's principal and the owner of Blackacre. By erroneous interpretation of the legal effect of the telegram, both parties believe that it authorizes A to sell Blackacre. B pays A for Blackacre. B is entitled to restitution from A unless C ratifies or A, before learning of the mistake, pays C the money.
>
> 2. Same facts as in Illustration 1, except that B sends the money to C. B is entitled to restitution from C, unless C ratifies.

Restitution (First) of Restitution § 47 (1937) (emphasis added). In either event – whether he had come into possession of the money or not – the principal is not entitled to the money. This

authority belies Novell's argument (at 2-3) that the precedent turns on whether the agent had already "properly remitted" the fruits of the contract to the principal. The illustrations make clear that there is no requirement that an agent must remit the fruits to the principal before the principal's lack of entitlement to them can be resolved. Novell does not – because it cannot – cite any case holding that a principal can recover the fruits of a contract that the principal chose to disavow as unauthorized. The precedent says the exact opposite.

In addition, any contract executed by a party without the authority to execute it is "void."[2] Novell (at 4-5) thus unsuccessfully seeks to downplay the significance of the "unremarkable principles" it purports to summarize from the cases SCO has cited: A void contract is "no contract at all,"[3] but rather an unenforceable promise.[4] The law provides that

[2] CSX Transp., Inc. v. City of Garden City, 325 F.3d 1234, 1240 (11th Cir. 2003) (citing authority); Prescott v. United States, 731 F.2d 1388, 1393 (9th Cir. 1984) (same); Emerson v. Labor Investment Corp., 284 F.2d 946, 949-50 (10th Cir. 1960) (same); SBRMCOA, LLC v. Bayside Resorts, Inc., No. 2006-42, 2007 WL 1795732, at *5 (D.V.I. Apr. 18, 2007) (Ex. B) (same); CSX Transp., Inc. v. City of Garden City, Ga., 391 F. Supp. 2d 1234, 1239 (S.D. Ga. 2005) (same); Demko v. Luzerne County Community Coll., 113 F. Supp. 2d 722, 729-33 (M.D. Pa. 2000) (same); Byrd v. Martin, Hopkins, Lemon and Carter, 564 F. Supp. 1425, 1428-29 (W.D. Va. 1983) (same); Poway Royal Mobilehome Owners Ass'n v. City of Poway, 149 Cal. App. 4th 1460, 1473 (2007) (same); St. Charles County v. "A Joint Bd. or Comm'n", 184 S.W.3d 161, 165-66 (Mo. Ct. App. 2006) (same); Pierce County v. Wash. Shellfish, Inc., 126 Wash. App. 1020, 2005 WL 536097, at *3 (2005) (Ex. C) (same); Miller v. Marshall County, 641 N.W.2d 742, 750-51 (Iowa 2002) (same); Red Dog Saloon v. Sedgwick County Bd. of Comm'rs, 33 P.3d 869, 871 (Kan. Ct. App. 2001) (same); Failor's Pharmacy v. Dep't of Social and Health Servs. v. Dep't of Social and Health Servs., 886 P.2d 147, 153 (Wash. 1994) (en banc) (same); Weese v. Davis County Comm'n, 834 P.2d 1, 3 (Utah 1992) (same); In re Estate of Griffin, 812 P.2d 1256, 1258-59 (Mont. 1991) (same); Vt. Dep't of Pub. Serv. v. Mass. Municipal Wholesale Elec. Co., 558 A.2d 215, 220 (Vt. 1988) (same).

[3] Sandvik AB v. Advent Int'l Corp., 220 F.3d 99, 109 n.7 (3d Cir. 2000); accord Lum v. Kauai County Council, Civ. No. 06-00068 SOM/BMK, 2007 WL 1482403, at *3 (D. Haw. May 18, 2007) (Ex. D); In re Donnay, 184 B.R. 767, 784 (Bankr. D. Minn. 1995); United States ex. rel. Gulbronson v. D&J Enters., No. 93-C-233-C, 1993 WL 767689, at *7 (W.D. Wis. Dec. 23, 1993) (Ex. E); Gull Labs., Inc. v. Diagnostic Tech., Inc., 695 F. Supp. 1151, 1154 (D. Utah 1988).

"when a contract is void, it is as if the contract never existed."[5] Under a void contract, as shown in SCO's opening brief and herein, the counterparty who made payments under the purported agreement is entitled to those payments.

C. Novell's Hypothetical Does Not Come out as Novell Assumes It Should.

Novell offers a hypothetical factual scenario that serves only to underscore that, alleging SCO's lack of authority, Novell cannot prevail on its claims for money. In that hypothetical, Novell has Scott selling Nathan's car without Nathan's permission – but where Scott and Nathan are merely "friends." As a fundamental matter, Novell thus side-steps a core premise of its own allegations – that Novell and SCO have a principal-agent relationship.

In any event, the precedent illustrates that Novell's own hypothetical would not be resolved as Novell rhetorically proposes it should be, whatever the relationships between Nathan and Scott. If Nathan brought suit and alleged that Scott lacked the authority to sell the car, these results would follow:

- Where Nathan is an alleged principal, having declined to ratify Scott's sale of the car, Nathan would not have triggered the legal relations "as between" himself and Scott that would make Scott subject to a fiduciary duty to account to Nathan. (See Part I.A, above.)

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[4] See 1 Williston on Contracts § 1:20 (4th ed. 2007) ("Void promises are not legally binding, have no legal effect, and, therefore, are not contracts."); Restatement (Second) of the Law of Contracts § 7 (1981), Comment a (an unenforceable promise "is often called a void contract," "such a promise is not a contract at all," and "[i]f the term 'contract' were defined to refer to the acts of the parties without regard to their legal effect, a contract could without inconsistency be referred to as 'void.'").

[5] Laborers' Pension Fund. v. A&C Environmental, Inc., 301 F.3d 768, 779 (7th Cir. 2002); accord Bd. of Trustees of the Masons and Plasters Pension Fund Local 56 Dupage County, Ill. v. O'Donnell Plastering, Inc., No. 01 C 9257, 2003 WL 174207, at *4 (N.D. Ill. Jan. 27, 2003) (Ex. F).

- Where Nathan is merely Scott's friend, the necessary premise of Nathan's suit means the sales contract is void. It would be as if the contract never existed, so that Nathan would not be entitled to the sales proceeds. (See Part I.B, above.)

Under either set of facts, Nathan would have no right to the money paid for the car. Otherwise, Nathan would get the money paid for a car that Marty could not even keep, because he actually never bought it – a truly surprising result. Most relevant to SCO's Motion, Nathan's allegations would not create any scenario under which he could have the money at issue.

II. IN THE ALTERNATIVE, NOVELL'S CLAIM FOR DECLARATORY RELIEF IS IMPROPER AND MUST BE DISMISSED.

Novell seeks to reserve the right to ratify the SCOsource Agreements, contending without citation (at 1) that whether to ratify "is not a choice that Novell needs to make now" and (at 5) that "Novell is under no obligation to decide now whether to ratify SCO's improper acts." These arguments are wrong.

First, contrary to its uncited legal argument, Novell clearly did have the obligation to choose whether to ratify the Agreements. Novell was obligated to "promptly repudiate" SCO's authority to execute the SCOsource Agreements "within a reasonable time" – a matter of "months" – after learning of them.[6] Novell cannot now reverse course, whatever the resolution of its claim for declaratory relief at trial. Indeed, Novell cites no authority even suggesting that a

[6] Dodson Int'l Parts, Inc. v. Hiatt, No. 02-4042-SAC, 2003 WL 22327176, at *13 (D. Kan. Sept. 25, 2003) (Ex. G); Inamed Corp. v. Kuzmak, 275 F. Supp. 2d 1100, 1119 (C.D. Cal. 2002); Merex A.G. v. Fairchild Weston Sys., Inc., 810 F. Supp. 1356, 1370-71 (S.D.N.Y. 1993); Heller Ehrman White & McAuliffe v. Price, No. A106899, 2005 WL 2293512, at *6-7 (Cal. App. Sept. 21, 2005) (Ex. H); Norcal Mut. Ins. Co. v. Newton, 84 Cal. App. 4th 64, 78-79 (Cal. App. 2000); Riss v. Angel, 934 P.2d 669, 683 (Wash. 1997); Moran v. Knights of Columbus, 151 P. 353, 360 (Utah 1915).

principal can use a trial to determine whether to make the binding decision on whether to ratify the allegedly unauthorized contract at issue.

Novell therefore is wrong in contending that SCO has merely manufactured Novell's obligation to have made such a choice years ago. In fact the Tenth Circuit long ago observed that, faced with the choice of whether or not to ratify, "the principal is impaled on the horns of a dilemma." Maryland Cas. Co. v. Queenan, 89 F.2d 155, 157 (10th Cir. 1937); accord First Nat'l Bank of Cicero v. United States, 625 F. Supp. 926, 932 (N.D. Ill. 1986). Yet "when the principal has no avenue through which to claim ownership of the disputed property except through its agent," it must ratify (and accept the consequences flowing from that ratification) to claim such ownership. Cicero, 625 F. Supp. at 932.

Second, even in trying to reserve the right to ratify the Agreements, Novell conflates the narrow, backward-looking declaratory relief it seeks with a general, forward-looking declaration. The declaratory relief Novell actually seeks at trial is improper. SCO showed in its opening brief that where a party seeks a declaration that amounts to an "advisory opinion" or that would apply to only a "hypothetical state of facts," the declaratory claim fails. (SCO's Opening Mem. at 9-10.) That is precisely the type of declaration Novell seeks through its arguments in its opposition brief. The question of whether SCO had the authority to execute the SCOsource Agreements would be relevant only if, after trial, Novell were to decline to accept any recovery on its claims for money, and only if, at the time, the Court were to conclude that Novell had exercised its right to choose whether to ratify within a reasonable period of time. The record thus leaves no doubt that Novell is seeking a declaration regarding only a hypothetical state of facts.

Novell as much as admits that it seeks an advisory opinion, maintaining without citation (at 5) that "one might reasonably expect Novell to wait until the propriety of SCO's acts is resolved by this Court before it makes any decisions regarding the SCOsource licenses," and (at 7 n.5) that "a decision by this Court that SCO did have the authority to enter into the agreements renders any ratification decision-making unnecessary." Novell's uncited argument is wrong – as an alleged principal, Novell was obligated to make the referenced decision well before trial; it cannot base that decision on how its claim for declaratory relief turns out.

Finally, even under Novell's apparent argument that the solely backward-looking declaratory relief its seeks is somehow the same as the separate, forward-looking relief it seeks in the same Fourth Claim for Relief, at a minimum the Court should dismiss those portions of Novell's claim that relate to the Sun and Microsoft Agreements. There is no evidence at all that the unique circumstances under which those two agreements were negotiated are likely to recur; the propriety of SCO's execution of these agreements has no bearing on future Linux-related agreements of the sort that Novell says it is concerned SCO may execute.

CONCLUSION

SCO respectfully requests, for the reasons set forth herein and in SCO's Opening Memorandum, that the Court dismiss Novell's Sixth, Seventh, and Eighth Claims for Relief or Novell's Fourth Claim for Relief.

DATED this 24th day of April, 2008.

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CERTIFICATE OF SERVICE

Plaintiff/Counterclaim-Defendant, The SCO Group, Inc., hereby certifies that a true and correct copy of the foregoing Reply Memorandum in Support of SCO's Motion for Judgment on the Pleadings on Novell's Claims for Money or Claim for Declaratory Relief was served on this 24th day of April, 2008, via CM/ECF to the following:

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