CRN Interview: SCO's Darl McBride and Chris Sontag

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By Barbara Darrow,
CRN

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*SCO CEO Darl McBride and Senior Vice President Chris Sontag met with **CRN** Industry Editor Barbara Darrow and **VARBusiness** Senior Executive Editor T.C. Doyle in Las Vegas. The conversation took place just hours after SCO said it made its chief litigator, David Boies, a stakeholder to the tune of 400,000 shares plus $1 million dollars. Earlier this year SCO charged that IBM had illegally turned over Unix code to the Linux community. Tuesday, SCO said it will likely sue an end-user company using the Linux code at issue in the suit. The SCO-IBM case is slated to hit a Utah courtroom in 18 months.*

CRN: You're paying David Boies [of Boies, Schiller & Flexner LLP] about $9 million to pursue your claims against IBM?

Darl McBride: We are giving him 400,000 shares of stock and $1 million in cash. When I said we have $60 some million in cash [on hand at SCO], reduce the cash by $1 million and we take non-cash charge. David comes on, he's now a shareholder, he's rowing with us, and let's face it, he's added significant value to our company since February. Our stock was around a buck, now it's $14. That's some of the best money we've spent, not even money, some of the best stock we've issued. Now we're broadening our scope and going after the cleanup project. The breadth of damage that's been done here, it's like cleaning up the Exxon Valdez... the code violation that is going on inside of Linux between derivative work, copyrighted work, it's not unsubstantial.

CRN: Can suing customers, as you've said you will, be good for any vendor?

McBride: First it's not our customers. I would say we're suing end users. There are only two industries who use the term 'users,' computers and drugs. Not sure if there's a connection there. But the point is, we're not suing our customers. We are going after end users of Linux and I think there's a slight but significant difference there.

CRN: When you talk to your VARs, partners, integrators... what are they saying about this legal battle? Is it confusing their market?

McBride: It's a range. Those who are directly selling SCO Unix products, are cheering us on, saying go, fight, win. Those who have drifted over to the Linux camp are confused. They don't know how to deal with this... 'What do we do?' It depends on where they are in the process.

CRN: Are you trying to evangelize them to speak out in your behalf? It's clear the open source crowd needs no encouragement to tell their side of the story.

McBride: My first reaction was we needed to create a counterbalance [to the vocal open sourcers]. We're on the side of the silent majority...but at the end of the day it's around who's right. We're rock solid on our claims... and we're not sitting here day in day out trying to counter the stones being thrown at us. We have a business to run. Our employees are reenergized around the movement back to Unix, reenergized around the role SCO is playing... . Our roots in the Unix business are strong and won't be blown over by a little bit of Linux wind.

CRN: Conspiracy theorists say you guys are acting as Microsoft's pawn against open source and the General Public License [GPL]. Can you comment?

McBride: The funny part is we didn't even talk to Microsoft about this outside the normal public interest level things... when we talk to them it's about what's happening in the marketplace. [I know] there is this feeling that something's happening here... . It's funny when I talked to IBM earlier this year, before we did anything, it wasn't even clear where the IP problems were. We just said we were going to start investigating IP issues, and IBM said, 'You're just giving Bill Gates an early Christmas present.' Bill Gates? This is about our IP! What are you talking about? This was the immediate reaction at IBM and the open source guys. Unfortunately for them, it's just not reality.

If people want to talk about conspiracy theories, they should spend some time poking what IBM, SUSE and Novell are talking about and what the 'Chicago 7' talked about in Chicago in July [2003. That was a group of companies with] a half a trillion dollars in market cap talking about what to do about SCO.

CRN: What is the 'Chicago 7'?

McBride: All the big guys, HP, IBM, Oracle, etc. (For more on the Chicago 7, see story.) Or look at the massive amount of money IBM is pushing into Linux companies all over the world. They should start a division in heart lung machines [to support] all those little companies

IBM is the master of creating an illusion that they're being attacked by this big brutal bully SCO when they're the ones attacking us. They're the ones doing all the behind-the-scenes work.

CRN: What do you see as the IBM/SUSE/Novell conspiracy?

McBride: We file a suit against IBM and we get a letter from Novell cc:ing IBM's legal counsel? Hmmm interesting.

We're protecting our IP and it's turned into a bar-room brawl. What's at stake here at the end of the day is not just between SCO and IBM, it's what's in the balance for the computer industry. Is the future of software free or a traditional license model and the outcome will have a lot of impact on the industry going forward.

CRN: So is the IBM case becoming a test of the GPL?

McBride: We early on looked at GPL-related issues and felt it was an Achilles heel for IBM but we didn't open them up initially. We didn't want to confuse a clear-cut contract issue [with IBM] with the untested GPL and other issues. But when IBM dragged GPL onto the table, our lawyers started sharpening their steak knives. 'Ok, if that's what you want to talk about , we'll talk about it.'

IBM will have a lot of problems trying to hide behind the GPL. Basically the GPL is countering U.S. Copyright law. Is IBM on the side of free software while they are one of the largest IP and IT firms in the world trying to protect their own patents and copy rights? It's just the most bizarre juxtaposition... . They're supporting something that's very unfriendly to copyrights.

CRN: Oracle, IBM and other software vendors say they're bleeding the cost out of the operating systems with Linux and hardware with standard, commodity gear, but they're not cutting the price of their own software.

McBride: That's the whole point. 'Let's bleed it out of the database, let's bleed it out of the apps. Lets have hardware all free this year. Let's alternate, we'll do software this year, next year you do hardware.'

It's a weird thing and what it is really is business competition. Underneath all this is hard-core capitalism. They're trying to drive us out of business and we're fighting back. The good news is we have the U.S. Copyright Office on our side to fight

with.

VAR Business: Other than the suit, how's business?

McBride: That's the great untold story no one even asks about. We have over two million servers actively running today. Customers continue to come to us. We have laid out a growth map that will be significant for our customers. In the next year expect Legend, which will take OpenServer and update it. Longer term, expect SVR 6, which will be 64-bit Unix on Intel. That is a few years out.

As we look at monetizing this two-million-user installed base, we can sell product for a $800 to $1,000 dollars, whatever. We're talking about a couple of billion dollars in upgrade opportunities.

From a financial standpoint. The first part was cleaning the company up. We've done that. Going forward we have three dials. The core business, we think that's bottomed out and there's upside now with new products coming. We haven't had a new product in our OpenServer base in years and years.

The second dial is the 2.5 million Linux servers out there today that are paired with our intellectual property in them. We have a licensed product $699, $1,399. Chris [Sontag] is driving that and that's another multi-billion-dollar revenue opportunity

The third bucket has to do with the IBM settlement. We filed that at $3 billion. Every day they don't resolve this, the AIX meter is still ticking....

That's in a Utah courtroom 18 months out. That's a down the road revenue opportunity but the first two dials are going right now, and today's announcement today with Boies will really help move the second dial along.

VARBusiness: Have you seen any movement on IBM's part to cease additional AIX development.

McBride: Right now, we're talking about the Linux base. We're a little company we have to choose our battles. Our goal is to take the Linux thing and get that tightened down and then swing back around on AIX. We're sort of fine to let the AIX thing tick, because the longer it goes, when we actually end up in courtroom, we can go back to June 13, 2003, and add damages. We're sort of fine to let that one run. I don't sense they've stopped shipping AIX and both sides right now are kind of on the Linux battlefront.

VARBusiness: What's the issue here?

McBride: It's that they've taken a substantial amount of our code is what creates the battleground. It's interesting to hear Red Hat speak at financial conference yesterday and their comment is, 'We're really scaling Linux up. Linux is really growing up.' If you take IBM out of the equation, Linux would not be growing up, it would not be SMP-enabled, it would not be multi processing, scaling up to hundreds of servers. It is IBM that is enabling that.

VARBusiness: What about others? Sun says they contribute more source code than anyone.

McBride: Sun even though they have the broadest rights of any Unix licensee out there, has been careful to not contribute things that would be outside their license. IBM's been the opposite. It has very limited rights but has been dumping substantial amounts of code. We have a very good relationship with Sun.

CRN: When did Sun sign its licensing agreement with you?

McBride: Originally they signed one back in '94, [then] another one in '99, another deal earlier this year. It's been an ongoing thing.

VARBusiness: Are customers changing their Linux purchasing pattern since SCO sent out warning letters?

McBride: A research report came out saying 80 percent of users had not slowed down. Our take on that is 20 percent have. So one out of five. We sent out our letter three to four months ago and in that period, one out of five have changed.

We think that's significant. We only mailed letters out to 1,500 companies. I would argue that is one out of five out there...it could be 100 percent of all[the companies] we sent it to, we don't think that's actually the case. Anecdotally, I can tell you... it has an impact. People are concerned. One transportation company said, 'We don't want to be on the wrong side of you guys on this. What do we do to get clean?'

We think as we head down this path of license or litigate, if look at what we've done over past three months, [it's been] pretty soft in reality. We've focused on playing defense against IBM and Red Hat through August and September. We focused on getting some money raised in October, we wanted our money base underneath us for the fiscal year. We got our legal case in place, taking care of business in defense of other suits. Now it's time to go back on offense.

I think where the barometer is going now, I think you'll see some increased interest in Chris's licensing program

VARBusiness: At the end of the day are you guys going to do to Linux what was done to Napster?

McBride: Our goal is not to blow up Linux. People ask why we don't go after the distributors...'If you have such a strong case, why not shut down Red Hat?' Our belief is that SCO has great opportunity in the future to let Linux keep going, not to put it on its back but for us to get a transaction fee every time it's sold. That's really our goal.

To the extent that we have to take it down and put it on its back, we're fully prepared and willing to do that. The thing about going after end-users is it doesn't shut down the flow of Linux. If you look at the GPL, it couldn't be more clear, they either have to pull [the offending code] or shut down the distribution. The things we're laying claim to are things you can't pull out very easily....it's very difficult to yank this stuff out. We're not actually shutting down the flow of Linux, just cleaning it up at the end user level.

[When I came aboard at SCO I looked at this issue of code and asked:] 'Why don't you guys do this?' They said, 'Because the Linux community will get mad at us.'

I tell you what, I'll give you the Linux community getting mad at us vs. shareholder value. That was the trade off. They were absolutely right, the Linux community got mad and we were right, shareholder value went up. The last time I checked the CEO was in charge of shareholder value, not standing around the campfire singing Kumbaya with the Linux world. So far, I'm pleased with where we're going..

CRN: The whole issue of customer lawsuits... you will be suing someone within 90 days?

McBride:They said within 90 days [this morning] but I would qualify that and say I'll be surprised if we get beyond 60 days.

CRN: HP I believe is the only vendor who's talked about indemnifying customers, if you guys sue an HP customer, what happens?

Chris Sontag: Well. HP put a lot of provisos in place [to qualify for indemnification.] You have to be an HP customer on HP hardware. You have to have a support agreement with HP which very few of their customers have. And you can't modify the code which may not be a huge issue because a very small number of commercial end users have wanted to modify the code anyway.

If I were a commercial end user independent of anything else, given the nature of the GPL I would avoid modifying the code, I would avoid doing anything that could be considered a distribution of my application. If I'm Merrill Lynch and have a trading application proprietary to Merrill Lynch and deploy it across all my trading desks, if that deployment occurred where the Linux OS and app are distributed togetherm there are arguments that Merrill would have to provide their proprietary trading application in source form to everyone. That's a problem. I'm sure all of Merrill's competitors would love to get that but it's hard for a company to be financially viable when all of the basises are shared.

One of the economic issues in general with Linux under the GPL is there's no ability to carve out and contribute some things and hold back stuff I consider valuable.

CRN:How about the hybrid model like MySQL, where they offer a commercial and GPL version of their software?

Sontag: Even those may ultimately be questioned . There's an issue of what's considered a distribution and just the vagaries of the GPL that you don't really know what you're dealing with. I hear people pontificating on what they think the GPL means, and others argue almost 180 degrees the opposite saying THIS is what the GPL means and the reality is they could both be right but there is no case law nothing on the GPL so therefore you don't know who's right.

CRN: Is the IBM case a test of the GPL or not?

Sontag: SCO had been avoiding testing the GPL. That' why we didn't take action against the distributors. However when IBM added the GPL to their defense, that necessitates that we take action in our case against the GPL and given that no case law on GPL and the weak wording it has, it's not a good defense on IBM's part. I scratch my head sometimes about why they would try to use the GPL as a shield.

Back to your question, yes we'll probably now be taking action against the GPL and given the fact that Novell has acquired SUSE and Red Hat has sued us we're likely now to be taking actions if we so choose against the distributors. It really ends up coming down to the end users who you have to focus on even if you don't want to because of how the GPL structures the relationship. There is no warranty, nothing with the developer, nothing with the distributor, the liability rests with the end user. That's how the GPL is written. It makes it hard for me to understand why people would want to jump on a supposedly free operating system that isn't free anymore. It's not such a good deal anymore.

CRN: Is it true you're using Samba in OpenServer?

Sontag: SCO has for a long time has been a participant in many Open Source projects and has made contributions. We have not contributed our System V code into open source but we have been active participants in many open source activities. We don't have an issue with open source, we have an issue with open source being hijacked for the use of certain companies or individuals to inappropriately contribute a lot of our IP into a given environment. So the concept of companies getting together and sharing source code and working together is not an issue for us and we've participated in that and benefited from a number of projects including Samba and continue to do so. We haven't identified any specific IP issues with Samba and that's why we continue to work with it. But if there were issues in the future we'd make appropriate decisions then. We've put some open source components into our products and likely will continue to do so in the future. That's not the issue, the issue is the GPL and its pushing IP liability issues unfortunately to the end user when they were likely not the ones causing the problems and those who've inappropriately taken our IP and contributed it predominantly Linux in violation of our contracts, in violation of our copyrights.

CRN: Have you identified exactly what code is at issue here?.

Sontag: We've identified a lot of different things. Early on when we filed against IBM, people wanted us to show the code, even though we're fighting a legal case and that's where it's appropriately vetted, we decided to take at least one example and show that. We had to do so under NDA, because if you're comparing our System V code, it is not released without confidentiality agreements. If you sign an NDA -- a number of journalists, analysts and customers have seen the example we showed -- a substantial amount was a cut and paste job, a few lines changed, but substantial body. You don't have to be a programmer at all to see copying had occurred. It wasn't just ten lines of code, that example was over 80 to 100 lines of code. Later some of the Linux people said that code shouldn't have been there, Bruce Perens said it was development problem and 'we've taken it out.' My analogy is [that's] like a bank robber with posse in pursuit swinging back by the bank and throwing the money back in... .

In that one example, copyrighted code had been misappropriated and there's substantial benefit out there that has still not been rectified. There are other literal copyright infringements that we have not publicly provided, we'll save those for court. But there are over one million lines of code that we have identified that are derivative works by IBM and Sequent that have been contributed into Linux that we have identified and there's been no effort by Linux leaders to start acting and rectify that situation.

It's kind of hollow words that we are not showing code, because we have shown examples and if we keep showing it, they'll just take that out and say 'no harm no foul.' That doesn't solve the problem.

CRN: Why in the world would any company take on IBM, which probably has more legal resources than any other company?

Sontag: They have more attorneys than we have employees. But we believe we have a very strong legal position or we would never have filed. Taking on the absolute largest IT and IP organization on the face of the planet that is 10,000 times our size is not something you take on lightly. However, we felt we had a very strong legal position on an IP basis for the legal claims we made.

From the start we took the position that we have to be willing to take this all the way to full legal conclusion and have been structuring the company such that we're financially profitable we're accreting cash. In the last year we've gone from almost no cash to more than $60 million in cash. Core operations are financially profitable. So we're now in a very good position to take this to full legal conclusion if necessary. Now, if there is an appropriate legal settlement that we think is reasonable and advantageous to our shareholders certainly we'll consider that, but we have to assume we take this to full conclusion and it may very well happen

CRN:IBM has shown no sign of negotiating?

Sontag: No.

McBride: They have more attorneys than we have employees. They have those [Cravath, Swaine and Moore] guys and their own people .What they said when they first saw the lawsuit was that 'the skies over Utah would be blackened with attorneys before this is all done.'

CRN: So, aren't you crazy to take this on?

McBride: This is a David and Goliath battle. The might and sheer size of IBM against the legal stone that we have, and it just so happens we have a very good legal stone and we have a guy named David [Boies] carrying the slingshot. So we like our chances.

The legal stone is clearly coming from David. He used to be with Cravath. It is an epic battle. The guy at Cravath supporting IBM used to work for David. [He's] Evan Chessler. So now you've got that sub-plot of the Grasshopper and Master thing.

CRN: How much of your $60 million in cash derives from those licenses from Sun, Microsoft, etc?

McBride: The combination of those is in the tens of millions of dollars. We're over $60 million in cash... .

CRN: How can you win suing customers and what happens if you go after HP customer?

McBride: The interesting scenario is, do you go after an HP customer or an IBM customer? That's what David is the master of. That's his final decision

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