

UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF DELAWARE

In re : Chapter 11
:
THE SCO GROUP, INC., *et al.*, :
:
Debtors. : Case Number 07-11337 (KG)
: (Jointly Administered)

Hearing Date: October 25, 2007 at 4:00 P.M.

**OBJECTION OF THE UNITED STATES TRUSTEE TO THE DEBTORS' MOTION
FOR AUTHORIZATION TO (I) CONTINUE PREPETITION SEVERANCE POLICY
APPLICABLE TO ALL EMPLOYEES AND (II) PAY SEVERANCE AND ACCRUED
BENEFITS TO EMPLOYEES TERMINATED POSTPETITION
(DOCKET ENTRY # 116)**

In support of her objection to the Debtors' motion for authorization to (i) continue prepetition severance policy applicable to all employees and (ii) pay severance and accrued benefits to employees terminated postpetition (the "Motion"), Kelly Beaudin Stapleton, United States Trustee for Region 3 ("U.S. Trustee"), by and through her counsel, avers:

INTRODUCTION

1. Under (i) (an) applicable order(s) of the United States District Court for the District of Delaware issued pursuant to 28 U.S.C. § 157(a) and (ii) 28 U.S.C. § 157(b)(2)(A), this Court has jurisdiction to hear and determine the Motion.

2. Under 28 U.S.C. § 586, the U.S. Trustee has an overarching responsibility to enforce the laws as written by Congress and interpreted by the courts. *See United States Trustee v. Columbia Gas Sys., Inc. (In re Columbia Gas Sys., Inc.)*, 33 F.3d 294, 295-96 (3d Cir. 1994) (noting that UST has "public interest standing" under 11 U.S.C. § 307 which goes beyond mere pecuniary interest); *Morgenstern v. Revco D.S., Inc. (In re Revco D.S., Inc.)*, 898 F.2d 498, 500 (6th Cir. 1990)

(describing the UST as a “watchdog”).

3. Under 11 U.S.C. § 307, the U.S. Trustee has standing to be heard on the Motion and the issues raised in this objection.

GROUND/BASIS FOR RELIEF

Administrative Expense Standard

4. 11 U.S.C. § 503(b)(1)(A) provides that, “[a]fter notice and a hearing, there shall be allowed administrative expenses, other than claims allowed under section 502(f) of this title, including the actual, necessary costs and expenses of preserving the estate” First, the U.S. Trustee leaves the Debtors to their burden to establish that the proposed payments under the Severance Policy represent the “actual, necessary costs and expenses of preserving the [Debtors’] estate[s].”

5. Second, the Severance Policy appears to be a hybrid plan which compensates an employee for termination in lieu of notice as well as provides credit for length of the employee’s service to the Debtors. Mot. ¶ 6 (summarizing Severance Policy). Under governing Circuit law, any payments relating to the length-of-service component of the Severance Policy are subject to proration into their pre-petition and post-petition components, with only the post-petition component receiving administrative expense treatment. See Former Employees of Builders Square Retail Stores v. Hechinger Inv. Co. (In re Hechinger Inv. Co.), 298 F.3d 219, 227 (3d Cir. 2002) (“Severance pay at termination based on length of employment is given in consideration of work performed both pre- and post-petition, and thus not all such pay is entitled to treatment as an administrative expense.”). Accordingly, the U.S. Trustee objects to the relief requested in the Motion to the extent it attempts to allow the length-of-service components of the proposed payments as administrative expenses of

the Debtors' estates without the required proration.

6. Third, the Debtors appear to suggest in paragraph 7 of the Motion that, while the "general parameters" of the Severance Policy are outlined in paragraph 6 of the Motion, the Debtors' Board of Directors has unlimited discretion to approve severance payments that exceed those "general parameters." Simply put, this Court should not be giving the Debtors' management a blank check to authorize severance payments in any amount going forward. Given that the Debtors' employees have no assurance that payments will exceed the "general parameters," limiting the Debtors' authority to authorize severance payments to those defined parameters provides some limits on the administrative cost of the Severance Policy. Alternatively, in the event that this Court were to permit the Debtors' Board of Directors (or any other entity) to authorize payments outside of the "general parameters," there should be subsequent notice of any such payments and an opportunity for objection to ensure that there is a check on administrative costs. The aforementioned limitations are particularly appropriate in light of the fact that an official committee of unsecured creditors has not been appointed in these cases.

*Calculation of Severance Payments to Insiders*¹

7. 11 U.S.C. § 503(c)(2) prohibits this Court from either allowing or paying severance to an insider of the Debtors under 11 U.S.C. § 503(b) unless two criteria are met: first, "the payment is part of a program that is generally applicable to all full-time employees;" and second, "the amount of the payment is not greater than 10 times the amount of the mean severance pay given to nonmanagement employees during the calendar year in which the payment is made." 11 U.S.C. §

1

Debtors' counsel advised undersigned counsel that the Debtors were withdrawing their request to make severance payments to the terminated Chief Financial Officer and the Vice President, Finance, without prejudice to their rights to renew their request for relief relating to those individuals.

503(c)(2)(A, B).

8. Given that the Debtors are seeking authority to make payments under the Severance Policy going forward, there will have to be subsequent notice with an opportunity to object for payments proposed to be made to those persons who are “insider[s],” including those persons who have been appointed officers under corporate bylaws. This Court does not know when future severance payments to “insider[s]” will be made – theoretically, they could be made in 2008 – and what the calculation of mean severance pay to nonmanagement employees will be as of that future point in time. Thus, the notice mechanism proposed by the U.S. Trustee is necessary to ensure that the limitation contained in 11 U.S.C. § 503(c)(2)(B) is observed.

Payment of Accrued PTO

9. At the “first day” hearing, the U.S. Trustee obtained the Debtors’ agreement that any pre-petition employment compensation or benefit payments paid pursuant to the “pre-petition wages” motion would be subject to the caps identified in 11 U.S.C. §§ 507(a)(4) and (a)(5). Provided that the same limitation governs the proposed paid time off “cash out” (inclusive of payments already made), the U.S. Trustee does not object to the grant of that relief.

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CONCLUSION

WHEREFORE the U.S. Trustee requests that this Court issue an order denying the Motion or granting other relief consistent with this objection.

Respectfully submitted,

**KELLY BEAUDIN STAPLETON
UNITED STATES TRUSTEE**

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