

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

DAVID KNOX and CAROLYN SCHACHT,

Plaintiffs, on behalf of themselves and all
others similarly situated,

-against-

CENGAGE LEARNING HOLDINGS II, INC.,
CENGAGE LEARNING, INC., and DOE AFFILIATED
ENTITIES 1-10,

Defendants.

No. 18 Civ. 04292 (GBD) (BCM)

ANSWER

Defendants Cengage Learning Holdings II, Inc. (“Holdings”) and Cengage Learning, Inc. (“Learning”), by their attorneys, Satterlee Stephens LLP, for their answer to the complaint of plaintiffs David Knox and Carolyn Schacht, respond and state as follows:

DEFENDANTS’ RESPONSES TO PLAINTIFFS’ ALLEGATIONS

1. Defendants admit that Plaintiffs are authors of textbooks published by Learning and are parties to publishing agreements with Learning regarding those textbooks. The agreements are attached as Exhibit A hereto. Defendants deny that Paragraph 1 accurately describes those publishing agreements, the actual terms of which include, *inter alia*, provisions fully assigning the Plaintiffs’ copyright to Learning and express grants of authority to Learning with regard to setting format, pricing, and marketing of the textbooks, and which do not include any terms limiting Learning to any particular revenue model. Defendants deny the remainder of the allegations in Paragraph 1.

2. Defendants admit that Learning and Holdings emerged from bankruptcy in 2014. Defendants deny that its business model “tramples on” or is in any way inconsistent with its authors’ rights; to the contrary, Defendants believe that the new Cengage Unlimited model will

increase sales and revenues (and, accordingly, royalties to authors). First, Learning is implementing Cengage Unlimited to address the decades-old problem of affordability in higher education. The traditional model of students buying course materials individually at high prices is broken. Sales continue to decline because students are not buying the materials. Students overwhelmingly state that course materials are overpriced and that the high costs are their top source of financial stress after paying for tuition. In addition, students state that the high price of course materials is an impediment to their educational goals. Cengage strongly believes that Cengage Unlimited will accrue enormous benefits to students and their ability to afford access to the quality works of authors such as Plaintiffs. Defendants deny the remaining allegations of Paragraph 2.

3. Defendants admit that Learning is introducing a new product called “Cengage Unlimited,” which will offer students unlimited access to most of Learning’s library for a flat, per-semester subscription fee. Defendants also admit that the extent to which subscribers actually utilize an author’s work is one of several factors that will go into calculating that author’s share of royalties from Cengage Unlimited. Defendants deny that this product in any way represents a “dismantling and frustrating [of] the business of selling Plaintiffs’ works”; rather Defendants expect Cengage Unlimited to increase sales (and, accordingly, the total author royalty pool) above where they would otherwise have been. Defendants also deny that including an author’s work in Cengage Unlimited is a breach of any author’s contract. Defendants deny knowledge or information sufficient to form a belief as to Plaintiff’s expectations as to their royalties but deny that Plaintiffs have any basis to expect them to “decline substantially”; Cengage’s expectation is that Plaintiffs will see increased royalties. Defendants deny the remaining allegations in Paragraph 3.

4. Defendants admit that digital courseware offerings include elements (such as multimedia, tests, and homework) that are not contributed by the textbook authors themselves, and that for purposes of calculating the revenue to which to apply the author royalty rate, Learning ascribes an appropriate value to these additional elements, which reduces the revenue base against which royalties are paid versus treating these elements as if they added no value to the courseware. Defendants deny that the value ascribed is arbitrary, improper or in violation of the author contracts. Defendants deny the remaining allegations in Paragraph 4.

5. Defendants admit that some of Plaintiffs' works experience some decline in per-unit royalties from 2016 to 2017, and further admit that Plaintiffs requested a full, third-party royalties audit from Learning despite having no audit right in their publishing agreements, which Learning declined to provide. Defendants deny that Learning has any policy or practice of refusing reasonable requests for data or information from its authors. Defendants deny the remaining allegations of Paragraph 5.

6. Defendants deny the allegations of Paragraph 6 and deny that Plaintiffs are entitled to any relief.

7. Defendants deny the allegations of Paragraph 7 and deny that Plaintiffs or any members of the putative class are entitled to any relief.

8. Defendants admit the allegations of Paragraph 8.

9. Defendants admit that venue is proper in this District and that they maintain an office at 75 Greene Street in New York. Defendants deny the remaining allegations of Paragraph 9.

10. Defendants admit that Learning, as successor to West Publishing, is party to the two contracts with David Knox described in Paragraph 10, but states that the first is dated

October 9, 1989 for a work entitled “Choices in Relationships” and the second is dated January 25, 1994 for a work entitled “Understanding Social Problems.” These contracts are attached as Exhibit A hereto. Defendants on information and belief admit that Knox resides in Winterville, North Carolina.

11. Defendants admit that Caroline Schacht is a party to the two agreements described in Paragraph 10 above, and on information and belief admit that she resides in Winterville, North Carolina.

12. Defendants admit that Learning operates as a publisher and distributor of higher education materials. Defendants deny that Holdings, which is a separate entity and parent company of Learning, has any contractual relationship with Plaintiffs or putative Class Members, nor have Plaintiffs pleaded any facts justifying piercing the corporate veil between the two Defendants. Defendants further state that Holdings is a Delaware corporation with its principal place of business in Boston, Massachusetts. Defendants deny the remaining allegations of Paragraph 12.

13. Defendants admit that Learning is a Delaware corporation registered to do business in the State of New York, and that Learning has an office at 75 Greene Street, but state that its principal place of business is in Boston, Massachusetts. Defendants deny the remaining allegations of Paragraph 13.

14. Defendants deny the allegations of Paragraph 14.

15. Defendants admit that Learning is a publisher, seller and distributor of textbooks and learning-materials for all educational levels. Defendants deny the remaining allegations of Paragraph 15.

16. Defendants admit that Learning enters into publishing agreements with its authors, but states that the specific terms vary from contract to contract. Defendants admit that these contracts typically involve a transfer of copyright to Learning. Defendants deny the remaining allegations of Paragraph 16.

17. Defendants admit that Learning is the successor-in-interest to numerous publishing agreements with authors. Defendants deny the remaining allegations in Paragraph 17.

18. Defendants deny knowledge or information sufficient to form a belief as to what Plaintiffs “relied upon” or “expected” but deny that they have taken or will take any actions contrary to Learning’s contractual obligations. Defendants deny the remaining allegations of Paragraph 18.

19. Defendants admit the allegations of Paragraph 19.

20. Defendants admit the allegations of Paragraph 20.

21. Defendants admit the allegations of Paragraph 21.

22. Defendants admit the allegations of Paragraph 22.

23. Defendants admit the allegations of Paragraph 23, except deny that Learning’s digital learning materials, while designed to support an author’s textbook, are necessarily “derived” from that work.

24. Defendants admit that the allegations of Paragraph 24 are substantially correct.

25. Defendants admit that Michael Hansen made the statements quoted in Paragraph 25 but deny that the allegations of Paragraph 25 are a complete and accurate description of the cited article.

26. Defendants admit that Michael Hansen made the statements quoted in Paragraph 26 but deny that the allegations of Paragraph 26 are a complete and accurate description of the cited article.

27. Defendants admit that the projection alleged in Paragraph 27 was part of Learning's operating plan upon its emergence from bankruptcy but deny that the allegations of Paragraph 27 are a complete and accurate description of the operating plan.

28. Defendants admit that Michael Hansen made the statements quoted but deny that the plaintiff-added emphasis in Paragraph 28 was a part of those statements, and deny that the allegations of Paragraph 28 are a complete and accurate description of the cited article.

29. Defendants deny the allegations of Paragraph 29, which have taken parts of quotes from the cited article and deliberately misrepresented their context. In particular, Defendants note that the article quoted Hansen as referring to *consumers* "reluctant" to adopt new formats, not authors.

30. Defendants admit that Learning intends to offer a subscription service called Cengage Unlimited, which will offer access to most of Learning's electronic catalog for a flat, per-semester fee. Defendants deny the remaining allegations of Paragraph 30.

31. Defendants admit that Learning's royalty calculations for Cengage Unlimited will include the Revenue Pool allocation described in Paragraph 31, but deny that this is a complete description of the royalty calculation. Defendants deny the remaining allegations of Paragraph 31.

32. Defendants deny the allegations of Paragraph 32. Defendants further note that the royalty calculation presentation reproduced in Paragraph 33 expressly states that allocation among revenue pools will be "based on their relative value to Cengage unlimited subscribers."

33. Defendants admit that the graphic reproduced in Paragraph 33 was produced by Learning and represents an accurate description of the intended royalty calculation methodology for Cengage Unlimited. Defendants deny the remaining allegations of Paragraph 33.

34. Defendants deny that the abridged quote in Paragraph 34 is a fair or complete description of the cited blog post. Defendants deny the remaining allegations of Paragraph 34.

35. Defendants admit that the anticipated royalty calculation for Cengage Unlimited will include as a factor the usage of a particular work by subscribers. Defendants deny the remainder of the allegations of Paragraph 35.

36. Defendants deny the allegations of Paragraph 36.

37. Defendants admit that they expect Cengage Unlimited to have a significant positive impact on both revenues and royalties. Defendants deny the remaining allegations of Paragraph 37.

38. Defendants deny the allegations of Paragraph 38.

39. Defendants admit that Learning has conducted a significant amount of outreach to its authors – including conference calls and webinars – in order to inform them about Cengage Unlimited and to answer questions and concerns. Defendants further admit that in some of these communications Learning has stated that because the point of Cengage Unlimited is to provide broad access to all of Cengage’s educational tools, authors will not be allowed to “opt-out” of the product. Defendants deny the remaining allegations of Paragraph 39.

40. Defendants deny the allegations of Paragraph 40.

41. Defendants deny knowledge or information sufficient to form a belief as to Plaintiffs’ “reluctance” to have their works included in Cengage Unlimited, but deny that

Plaintiffs have any reasonable basis for any such reluctance, and deny the remaining allegations of Paragraph 41.

42. Defendants deny the allegations of Paragraph 42.

43. Defendants deny the allegations of Paragraph 43.

44. Defendants admit that, as Plaintiff's publishing agreements include a full assignment of copyright to Learning, they necessarily authorize Learning to prepare electronic versions and digital courseware, and that these agreements provide for royalty payments to Plaintiffs, but deny the implication that the agreements in any way limit the ways in which the Plaintiffs' works can be sold. Defendants deny the remaining allegations of Paragraph 44.

45. Defendants admit that MindTap and other digital courseware package an author's work with supplementary materials, such as homework, quizzes, tests and multimedia materials designed to support the work and enhance the learning experience. Defendants deny the remaining allegations of Paragraph 45.

46. Defendants deny the allegations of Paragraph 46.

47. Defendants deny the allegations of Paragraph 47.

48. Defendants admit that digital courseware is one of the Revenue Pools used in the calculation of royalties for Cengage Unlimited. Defendants deny the remaining allegations of Paragraph 48.

49. Defendants admit that Learning typically provides Plaintiffs with a semi-annual statement of royalties. Defendants deny the remaining allegations of Paragraph 49.

50. Defendants deny the allegations of Paragraph 50.

51. Defendants admit that Plaintiffs requested a full, third-party royalties audit from Learning despite having no audit right in their publishing agreements, which Learning declined to provide. Defendants deny the remaining allegations in Paragraph 51.

52. Defendants deny the allegations of Paragraph 52.

53. Defendants deny the allegations of Paragraph 53.

54. Defendants deny the allegations of Paragraph 54. Defendants further state that, whether obligated or not, Learning has always provided reasonable and clear disclosure to answer good faith questions by its authors, including Plaintiffs.

55. Defendants deny the allegations of Paragraph 55.

56. Defendants deny the allegations of Paragraph 56.

57. Defendants deny the allegations of Paragraph 57.

58. Defendants deny the allegations of Paragraph 58.

59. Defendants deny the allegations of Paragraph 59.

60. Defendants deny the allegations of Paragraph 60.

61. Defendants deny the allegations of Paragraph 61.

62. Defendants deny the allegations of Paragraph 62.

63. Defendants deny the allegations of Paragraph 63.

64. Defendants deny the allegations of Paragraph 64.

65. Defendants deny the allegations of Paragraph 65.

66. Defendants deny the allegations of Paragraph 66.

67. Defendants deny the allegations of Paragraph 67.

68. Defendants deny the allegations of Paragraph 68.

69. Defendants deny the allegations of Paragraph 69.

70. Defendants admit that Holdings knows that Learning has publishing agreements with authors but deny that these authors are members of a legally cognizable class.

71. Defendants deny the allegations of Paragraph 71.

72. Defendants deny the allegations of Paragraph 72.

73. Defendants deny the allegations of Paragraph 73.

74. Defendants deny the allegations of Paragraph 74.

75. Defendants deny the allegations of Paragraph 75.

DEFENSES

By including a defense below, Defendants do not intend thereby to assume any burden of production or proof with respect to supporting facts that as a matter of law belongs to Plaintiffs, or any other burden not prescribed by law.

All references below to “Plaintiffs” refer not only to the named Plaintiffs but to members of the putative class as well.

FIRST DEFENSE (Failure to State a Claim)

1. The allegations of the complaint fail to state a claim upon which relief may be granted.

SECOND DEFENSE (Copyright Preemption)

2. Plaintiffs’ works come within the subject matter of copyright.
3. Plaintiffs seek relief, in part, that is the equivalent of one of the exclusive rights within the general scope of copyright.
4. Such relief is therefore preempted by the Copyright Act, 17 U.S.C. § 301(b).

THIRD DEFENSE (Economic Interest)

5. Learning is a wholly-owned subsidiary of Holdings.

6. Holdings has an economic interest in the affairs of Learning including, *inter alia*, its contractual relations with authors such as Plaintiffs.

7. Although Learning did not breach any author contracts, and Holdings did not procure any breach, any actions taken by Holdings were done in furtherance of its economic interest, and Plaintiffs have not alleged to the contrary.

8. Further, any actions taken by Holdings were not made with malice, fraud or illegality and Plaintiffs have not alleged to the contrary.

9. Accordingly, any actions taken by Holdings are privileged and not actionable as tortious interference.

FOURTH DEFENSE (Statute of Limitations)

10. Plaintiffs' claims are barred to the extent that they, or any part thereof, accrued outside of the applicable statute of limitations.

FIFTH DEFENSE (Waiver, Estoppel or Ratification)

11. Plaintiffs have been aware of, allowed, acquiesced in, and profited by allowing their works to be marketed and sold under circumstances that they now claim are breaches of their publishing agreements.

12. Plaintiffs' claims arising out of such circumstances are barred by doctrines of waiver, estoppel, and/or ratification.

SIXTH DEFENSE (Failure to Join Necessary Party)

13. One of the contracts pleaded in the complaint is for the work "Understanding Social Problems."

14. The lead author for that text is also a party to the contract, dated January 25, 1994, governing that work.

15. The relief sought by Plaintiffs would impair the lead author's interest in the work and her rights under the agreement.

16. The lead author is therefore a necessary party to this suit who has not been joined.

Dated: July 27, 2018

SATTERLEE STEPHENS LLP

/s/James F. Rittinger

James F. Rittinger

Glenn C. Edwards

Michael A. Cabin

230 Park Avenue, Suite 1130

New York, NY 10169-0079

(212) 818-9200

(212) 818-9606/7 (fax)

*Attorneys for Defendants Cengage Learning
Holdings II, Inc. and Cengage Learning, Inc.*