

Nortel's US Arm Pushes To Reverse \$7.3B Allocation Ruling

By **Matt Chiappardi**

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Law360, Wilmington (April 5, 2016, 10:03 PM ET) -- Nortel's U.S. arm pushed the Delaware federal court Tuesday to overturn the bankruptcy court's decision on how \$7.3 billion raised by liquidating the defunct Canadian telecom should be divided among affiliates across the world, arguing the ruling violated fundamental insolvency law and stretched equitable powers to the breaking point.

During a hearing in Wilmington, Jeffrey A. Rosenthal of [Cleary Gottlieb Steen & Hamilton LLP](#), attorney for the U.S. affiliate of [Nortel Networks Inc.](#), pounded the **lower court's ruling** with criticism, arguing that the decision to divvy the money up via a modified pro rata allocation method goes far beyond anything permitted by the Bankruptcy Code and calls into question how every multinational corporation, the majority of which are incorporated in Delaware, would be treated in Chapter 11.

"This decision is so contrary to the Bankruptcy Code, so contrary to the Third Circuit, that we need to get it right," Rosenthal told U.S. District Judge Leonard P. Stark. "The bottom line is: You have to follow the law."

Nortel's U.S. arm is appealing a decision reached by U.S. Bankruptcy Judge Kevin Gross in May after a monthlong cross-border allocation trial that took place simultaneously in Delaware and Toronto, with the two courtrooms connected by computer video feed, to decide how the \$7.3 billion pot should be divided among the telecom's units in Canada, the U.S., and countries in Africa, the Middle East and Europe.

Judge Gross ruled that the money should be split up on mostly a pro rata basis, based on claims against each of the units, a decision that was echoed in a separate opinion by Justice Frank Newbould of the Ontario Superior Court and did not jibe with any of the allocation schemes proposed by the multiple sides in the sprawling case.

The U.S. units **argued** that the scheme results in their creditors getting only roughly 14 cents on the dollar, compared with recoveries of close to 50 cents for both the Canadian and European units, even though the stateside arm would be getting a bit more than \$3 billion from the sale of Nortel's patent portfolio.

The stateside units also contend that Judge Gross overstepped the equitable powers given him by the Bankruptcy Code with his allocation scheme. The U.S. units argue that the money should be divided by

ownership rights in the particular assets sold, a notion Judge Gross rejected in his opinion when he found that development of Nortel's intellectual property was not the work of an individual affiliate but a collective effort of the company, and the proceeds should be allocated accordingly.

But Nortel's U.S. arm claims Judge Gross doesn't have the authority to impose such an allocation scheme under equitable bankruptcy court powers because he never heard evidence on fairness and equity during the trial, and his opinion makes extensive findings of ownership interests but doesn't apply them.

"What we were ultimately left with was a circular opinion," Rosenthal said in court.

Other creditor groups of Nortel's U.S. arm seconded its arguments, arguing that the stateside units were being penalized and that Judge Gross penned an opinion that essentially has no real explanation of what is fair and equitable in the situation.

Nortel's Canadian and other units pushed back against the appeal, arguing that their U.S. counterparts were missing the thrust of Judge Gross' opinion and that there was no real reallocation of property going on.

Judge Gross had ruled that ownership of the assets was shared among the global company, and while the Canadian and other units didn't get exactly what they wanted either, they were "prepared to live with it in order to get to distribution of assets," the Canadian debtors' attorney Ken Coleman of [Allen & Overy LLP](#) told Judge Stark.

The issue stems from the \$9 billion raised from the sale of major assets, including \$4.5 billion from a sale of its patent portfolio, after Nortel sought court protection in Canada, the United Kingdom and the United States in 2009.

The sides expedited the sale by agreeing to split the spoils at a later date, and about \$7.3 billion in proceeds ended up in an escrow account in New York with the issue going to trial after mediation failed.

On Tuesday, Judge Stark wondered if the issue ought to be certified straight to the Third Circuit, a move **Judge Gross had rejected** on grounds the issue wasn't yet ripe for the circuit court.

Judge Stark otherwise kept his card close to his chest, asking only questions to clarify the sides' positions and taking the matter under advisement.

Nortel's U.S. units are represented by James L. Bromley, Jeffrey A. Rosenthal and Lisa M. Schweitzer

of Cleary Gottlieb Steen & Hamilton LLP, and Derek C. Abbott, Andrew R. Remming and Tamara K. Minott of [Morris Nichols Arsht & Tunnell LLP](#).

Nortel's Canadian units are represented in the United States by Ken Coleman, Jacob S. Pultman and Laura R. Hall of Allen & Overy LLP, and Mary F. Caloway and Kathleen Murphy of [Buchanan Ingersoll & Rooney PC](#).

The appellate case is In re: Nortel Networks Inc. et al., case number 1:15-cv-00624, in the U.S. District Court for the District of Delaware.

The bankruptcy case is In re: Nortel Networks Inc. et al., case number [1:09-bk-10138](#), in the U.S. Bankruptcy Court for the District of Delaware.

--Additional reporting by Kurt Orzeck and Jonathan Randles. Editing by Aaron Pelc.