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## Working Capital: Nortel fast-tracking unlikely to bring speedy solution

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By Bert Hill, OTTAWA CITIZEN



July, 2009 file photo: Employees of the Nortel plant gather in front of the factory in Chateaufort, outside Paris, on July 15, 2009 after workers threatened to blow up the premises if their demands for compensation were not met. The workers of Nortel France, a subsidiary of the Canadian telecommunications firm Nortel, on compulsory liquidation since May 28, 2009, removed canisters of natural gas set up on the eve at their work site, prior to a meeting with Nortel managers this afternoon. Nortel, once Canada's largest company with activity in 154 countries, is in bankruptcy protection. Banner reads: "Nortel, "golden" bosses, ruined families."

### Photographed by:

BERTRAND GUAY, AFP/Getty Images

OTTAWA — A recent court decision putting the Nortel Networks bankruptcy nightmare on a fast track to trial might seem like welcome news.

But the result could be more pain for thousands of Nortel pensioners and disabled and former employees who took big financial losses, and more legal fights in the future.

Delaware and Ontario court judges last week told creditors with \$36 billion in claims chasing \$9.7 billion in Nortel assets to prepare for trial as early as this fall.

After a valiant mediation effort by Ontario chief justice Warren Winkler failed in January, the judges ordered combatants to produce a list of the big issues.

Not surprisingly, the big creditor battalions in North America came up with very short lists. Indeed, bondholders believed the complex trials could be wrapped by the end of the year because the issues have been clearly defined through three mediation efforts.

Alas, big creditors in Europe and smaller creditors in Canada and elsewhere are not nearly as confident: their issues are much more numerous and they fear the U.S. creditors will be the big winners. The problem is that the assets likely will be divided among the U.S., Canadian and European operating divisions based on binding local restrictions and cash reserves — not equally among contending creditors around the world.

The Canadian operations have relatively little cash and some huge claims to settle.

Diane Urquhart, an analyst assisting some Canadian Nortel disabled employees, said the deck is stacked against all Canadian creditors. "It is likely that the joint court hearing will result in an outcome where the U.S. creditors get \$1 per \$1 of claim, while Canada creditors get closer to 20 cents per \$1 of claim, in my opinion."

The race to judgment could create more unhappy creditors with an incentive to fight on, opening the door to future appeals and the leakage of more millions of dollars of Nortel assets to legal expenses. That is exactly the disaster scenario Winkler warned could happen.

There is a taste of the bitter future in new proceedings in the Delaware bankruptcy court. A group of 176 Canadian former employees are asking for the right to sue for a piece of Nortel U.S. assets to compensate for lost severance and other benefits.

The group, which includes Paula Klein, a former top executive in Nortel's Ottawa research operations and a leader in the bankruptcy battles, said Canadian employees "have experienced a great deal of loss and hardship" and the situation is unlikely to improve because "the U.S. is expected to be paid out at a higher dividend."

The effort makes sense, though its chance of success may be slim. The U.S. creditors are fighting the move, which goes to court later this month after getting delayed last week.

Any of three big issues could shipwreck Canadian pensioners, former employees and suppliers.

One of the most controversial is a claim by bondholders for their full \$4 billion in holdings because, they say, the bonds were guaranteed against both U.S. and Canadian assets. Plus they want about \$1 billion interest on the grounds that Nortel was solvent and capable of paying all its debts when it went into bankruptcy protection with \$2 billion in cash.

Next is a British pension insurance plan seeking \$1.335 billion for the cost of protecting the pensions of about 38,000 former Nortel employees. Finally, there are claims of up to \$10 billion by British and European creditors who believe Nortel's North American leadership diverted assets during the fight for survival.

The two big European claims have been rejected by the U.S. courts. But they are back for what some U.S. debt-holders call "a second bite at the apple." The courts will be hard-pressed to craft a decision that does not ignite a new round of appeals in European courts.

The big claimants conveniently ignore six other issues, defined by Ernst and Young, the court-appointed independent monitor. Among them are an \$18-million Ontario government environment claim to clean up a former Nortel plant in London and several court fights with former Nortel customers as well as with an insurance company over who pays the legal costs of former executives like Mike Zafirovski and former directors. Finally, there are disputes between various Nortel operations over some unsold Nortel assets and a myriad of complicated counterclaims.

One huge issue is the \$2.1-billion charge against Canadian assets that the U.S. operation will get to cover tax expenses triggered by the infamous Nortel accounting scandal. While the accounting problems put the nail in the Nortel coffin, the so-called scandal is very much in doubt after the courts threw out fraud charges against former chief executive Frank Dunn and others.

But that huge claim, agreed to between U.S. and Canadian operations early in the bankruptcy proceedings, will soak up limited Canadian cash and add to the suspicions of Europeans that they are the victims of an inside job.

The fact the Ontario and Delaware courts last week rejected the European plea for an international arbitration to settle the issues will just add to the sense of unfairness.

Meanwhile, Nortel just got partial exemption from a new Delaware bankruptcy court rule that requires insolvent outfits to fully disclose the costs when their law firms bring in more experts. That's right, Nortel won the right to quietly add to the roster of 29 law firms, asset sale specialists and restructuring experts in the U.S. proceedings.

It has also hired 13 Canadian law firms who so far have received \$254 million in fees — more than the \$208 million Nortel received for the sale of Carling Avenue campus.

Total legal spending in the U.S., Canada and Europe has reached \$861 million in the first four years of bankruptcy proceedings, up \$24 million in the last few months. The numbers are tabulated from Nortel records by Urquhart, the Toronto analyst.

The Delaware court agreed that Nortel can keep the new hiring under wraps for strategic litigation reasons. Disclosing the hiring of particular experts could tip off opposing lawyers on trial strategy.

However, the court denied Nortel carte blanche after the U.S. trustee, who referees bankruptcy proceedings, objected that the exemption could lead to abuses. Nortel must disclose the new hiring to the court and the trustee immediately and to everyone else once the trials are done.

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