

Nortel trial: Fraud trial hears changes in accounting standards impacted Nortel restatements

Published On Fri Feb 17 2012 , Toronto Star

[Email](#)

[Print](#)

[Rss](#)

[Article](#)

Michael Lewis Business Reporter

Nortel Networks Corp.'s accounting for revenue from complex, multi-year customer contacts was in focus Friday at the fraud trial of senior executives at the now insolvent telecom giant.

Under defence cross-examination, former Nortel assistant controller Karen Sledge agreed that changes in accounting standards governing contract accruals played a significant role in the Toronto company's sweeping restatement of its financial results in 2005.

"It's complex, for sure and there are many implications depending on how you recognize the contract and its liabilities," she said.

David Porter, lawyer for former Nortel chief executive Frank Dunn, said the company decided after its initial restatement in 2003 that it would utilize a legal option to apply the standard changes retroactively all the way back to 2000 "in the effort to get it right." He said the result was that some accruals on Nortel's ledger to account for warranty, product rebates and other costs incurred under sales contracts with its customers needed to be restated while some revenue was removed from the income statement or booked in a another period.

But Porter suggested the changes were simply an effort to make Nortel's revenue recognition treatment conform to the new standards under U.S. generally accepted accounting principles, or GAAP.

Dunn, former Nortel chief financial officer Douglas Beatty and ex-controller Michael Gologly were fired for "financial mismanagement" by the optical gear maker's board in 2004 and charged by the RCMP in 2008 with accounting fraud.

Robert Hubbard, chief prosecutor in the trial that began in Toronto January 16, alleges that the accused directed the release of hundreds of millions in excess reserves to fabricate profits and trigger so-called return to profit bonuses payments in 2003 to employees and senior managers.

Porter on Friday continued to present evidence that suggested Nortel's auditors were deeply involved in an effort to find business records that justified the release of the excess accruals to income, which had the effect in the first half of 2003 of lowering costs and boosting profits.

He presented memos and other documents that charted Nortel finance staffer's work to document specific accruals that had been flagged for review by outside auditor Deloitte and Touche LLP and a U.S. law firm hired by the Nortel audit committee as part of the review and restatement process.

Porter had introduced evidence that showed more than 200 Nortel control and accounting

personnel, 50 staffers from Deloitte plus technical specialists were brought in from accountancy Ernst & Young to work on Nortel's balance sheet review and restatement.

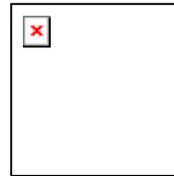
Nortel posted a profit in the first quarter of 2003 that triggered more than \$73 million in bonuses payouts along with stock awards to select managers. The surprise profit after more than eight quarters of steep losses led to a balance sheet review under direction of Nortel's audit committee and Deloitte.

The effort identified nearly \$1 billion in accruals for future expenses that had been improperly recorded and needed to be restated.

A few months later the company announced material errors in that restatement and said it would undertake another, more comprehensive revision of financial results for three and a half years starting in 2000.

The second restatement produced a substantial variation in revenue adjustments but Porter argued that the variance can be largely attributed to evolving circumstances and changes in accounting standards over the period.

[inShare0](#)



Nortel Not Ready To Provide Restated Results

By [Jennifer Hagendorf Follett](#), CRN

June 02, 2004 11:15 AM ET

Nortel Networks Wednesday said it's not ready to release restated financial results during this quarter.

The restated results date back to 2001. In a conference call on the status of the ongoing independent review of Nortel's accounting, President and CEO Bill Owens characterized the restatement as "of the highest importance."

"We will get this done as promptly as possible in line with doing it correctly, and we will fix our financial systems to report accurately and transparently in the future," Owens said. Owens, who joined Brampton, Ontario-based Nortel about a month ago in a flurry of personnel changes, pledged that the company will drive revenue growth, build up its cash balance and cut costs to address new competitors operating in low-cost labor markets, such as Chinese networking vendor Huawei Technologies.

"We will get through this accounting restatement and will do so in good shape," Owens said, adding that Nortel expects to grow faster than the overall telecommunications market.

Nortel executives couldn't give a timetable for the review's completion. To help speed the process, the company has brought in Ernst & Young to provide advisory services and additional accounting resources.

In addition, Nortel reiterated that it expects to report approximately a 50 percent reduction of previously reported earnings for 2003. The company also said it will report a loss for the first half of 2003, whereas it previously announced a profit for the period. Owens said Nortel expects no material impact to previously announced revenue figures or the company's cash balance.

At the end of April, Nortel fired President and CEO Frank Dunn and several other executives amid the independent review, which began in the fall.

The U.S. Securities and Exchange Commission and the Ontario Securities Commission have launched investigations into Nortel's finances. In May, the company also received a subpoena to produce documents for a federal grand jury in connection with an ongoing criminal investigation by the U.S. Attorney's Office for the Northern District of Texas, Dallas Division. In addition, 27 class-action lawsuits are pending against Nortel in the United States.

http://www.crn.com/news/networking/21400890/nortel-not-ready-to-provide-restated-results.htm;jsessionid=CztcYJfJNboAui4PTWecPw**.ecappj01