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Nortel fraud trial launches with not guilty pleas, allegations of a cookie jar culture

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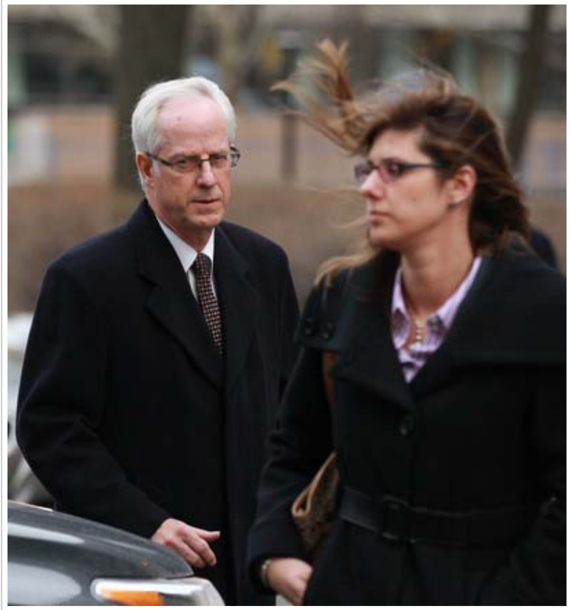
The fraud trial of former Nortel Networks Corp. executives began Monday with the prosecution alleging a “cookie jar” culture in which accounting reserves were repeatedly manipulated to meet thresholds and trigger bonus payouts.



Former Nortel CEO Frank Dunn leaves the Provincial Courts after the first day trial.

STEVE RUSSELL/TORONTO STAR

“They set their targets,” chief prosecutor Robert Hubbard said in his opening remarks before Superior Court Justice Frank Marrocco. “Then they went about doing whatever needed to be done to meet those targets.”

The accused, former Nortel chief executive Frank Dunn, former chief financial officer Douglas Beatty and ex-Nortel corporate controller Michael Gollogly, were fired by Nortel for cause in 2004 amid allegations of financial mismanagement. The RCMP laid fraud charges against the three men in 2008.

They are accused of manipulating Nortel’s financial reporting to trigger multi-million bonus payouts linked to the networking company’s return to profitability.

All three men entered pleas of not guilty at the start of the trial a spokesman for the Ontario Ministry of the Attorney General said could last more than six months.

None of the allegations have been proved in court.

The Crown said it has tabled a list of 27 potential witnesses, many of them Nortel finance department employees at the time of the alleged fraud in the early part of the last decade.

Hubbard said the prosecution will focus on testimony from about 12 key individuals, and present internal Nortel communications to demonstrate that the accused knew or should have known accounting entries that triggered a $1 billion restatement in 2003 were false.

He also said the Crown will call Canadian lawyers present during interviews with the accused by a U.S. law firm hired to probe Nortel’s accounting after the now-insolvent company reported a surprise profit in 2003.

Before the start of the trial Justice Marrocco dismissed a defense motion that would have required prosecutors disclose more detail on the allegedly fraudulent accounting entries that are the basis of the indictment.

Justice Marrocco said he is satisfied the Crown has sufficiently narrowed the focus in the two remaining charges to a limited series of transactions leading up to the first restatement of Nortel financial results.

That was followed by a second restatement less than six weeks later that the Crown alleges is evidence misuse of reserves continued even after Nortel had launched an investigation.

Hubbard said the accused were party to “discreet transactions” designed to shift in some cases comparatively small amounts of reserves to meet bonus targets.

He alleged the executives were acutely aware of the amounts needed to trigger special stock rewards and return to profit payouts. Hubbard alleged Dunn ordered release of accruals to turn an operating loss in 2003 into a profit. In on one case, the prosecutor said Dunn ordered reserves to be used to assure a profit according to both generally accepted accounting practices and Nortel’s own internal, pro forma accounting measures.

He also alleged the accused presented business outlooks to the company's board that were based on the manipulated accounts, adding the company's long time external auditors, Deloitte and Touche "certainly didn't see the real outlook."

The Crown is to resume its opening remarks Tuesday followed by the initial defense submissions. In a pre-trial submission last week Dunn's lawyer David Porter gave a preview of the defense case, arguing that a series of accounting restatements at Nortel were the result of accounting errors, and were not deliberate attempts to tailor results to meet targets.