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Nortel creditors watch in dismay as ballooning legal fees whittle away assets

Ex-employees and pensioners feel “left behind” as professional fees and expenses in the complex bankruptcy case rise above \$1 billion — and counting.

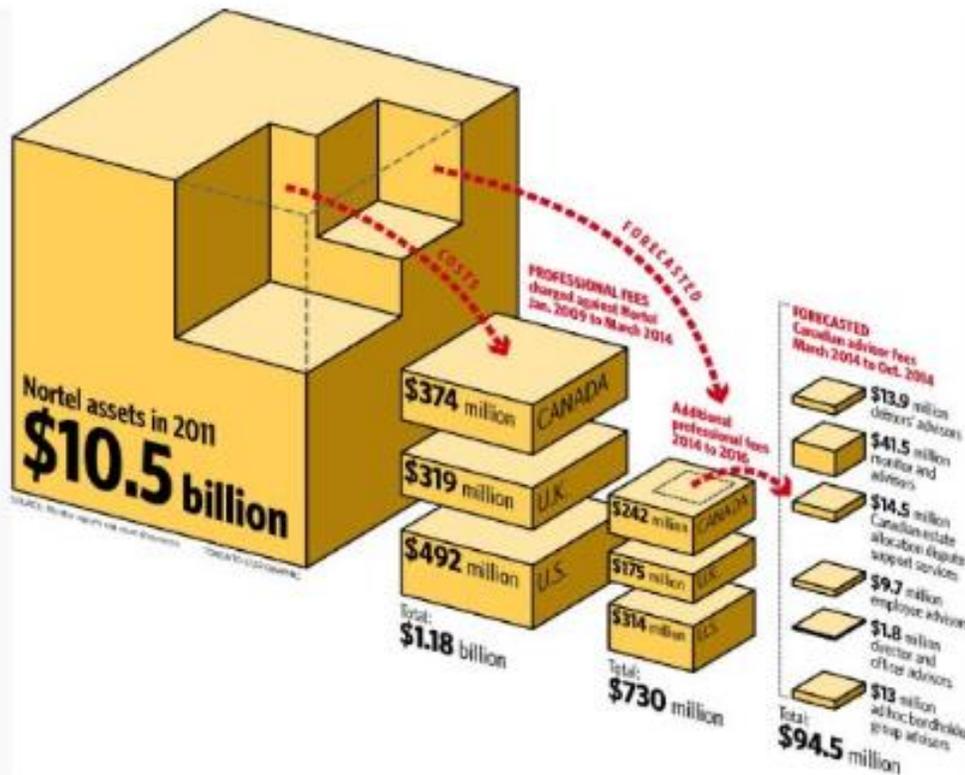


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Darren Calabrese / THE CANADIAN PRESS FILE PHOTO

Nortel pensioners rally in Toronto in 2010. Professional fees and expenses in the company's massive bankruptcy case now total more than 11 per cent of the \$10.5 billion that was available in 2011 for debtors and creditors.

By: [Michael Lewis](#) Business Reporter, Published on Mon Jun 23 2014



Law firms have eaten up nearly \$1.2 billion (U.S.) of Nortel Networks' remaining assets, leaving the company's retirees and ex-employees wondering if they'll ever get anything from the former tech powerhouse.

The fees and expenses so far total more than 11 per cent of the \$10.5 billion that was available in 2011 for dispersal to debtors and creditors, including about 22,000 former workers in Canada.

No one is alleging any wrongdoing in bills submitted by professionals in the exceedingly complex and time-consuming cross-border bankruptcy process, and judges have routinely signed off on invoices. But fees from lawyers and other professionals in the Nortel case have prompted Canadian bankruptcy monitor Ernst & Young Inc. to say it is "concerned about the significant costs." Ernst & Young said it has tried to streamline the process where possible.

For former Nortel workers in Canada, the continued bleeding away of the remaining \$7.3 billion available for distribution is excruciating.

"I'm really outraged at how we are left behind while we see lawyers making windfall profits," said Greg McAvoy, 61, a former senior manager at Nortel's wireless development centre in Calgary who went on long-term disability just before the company's bankruptcy in 2009.

"I blame the legal system. Judges should have been leaning on fees since day one. Ottawa should have stepped in. But the legal profession, the Insolvency Institute, the banks all opposed it."

He also noted that three failed mediation attempts have boosted the costs needed to ensure that the estate's assets are disbursed fairly.

After Nortel filed for creditor protection, its employees in Canada received no severance and saw their medical benefits and life insurance coverage terminated, according to Don Sproule, chair of a group fighting for the rights of the former workers.

In July 2011, Nortel pension administrator Morneau Shepell announced that pensioners in Canada would have their benefits slashed by as much as 70 per cent from former levels.

McAvoy, who has multiple sclerosis, was cut off from Nortel medical benefits in 2010 along with 353 other employees in Canada on long-term disability. He now has to live on a Canada Pension Plan disability income of \$1,147 a month.

Along with three other disabled colleagues, McAvoy filed a formal request last year with the Office of the Superintendent of Bankruptcy for an audit of the professional fees.

He said the superintendent, Bill James, refused to intervene, saying new bankruptcy rules and expanded powers became effective on Sept. 18, 2009, a few months after Nortel's collapse.

A spokesman for Industry Canada said public consultations have been launched in a review that will determine if the superintendent should have greater authority to examine and object to professional billings in bankruptcy cases.

Oversight of professional fees currently falls largely to the courts as administrators of insolvency law.

The so-called fees burn rate has jumped since January as lawyers geared up for the most expensive portion of the process: a trial linked by encrypted video and audio feeds that began in Toronto and Wilmington, Del., on May 12.

Bankruptcy watchdogs in the U.S. have rolled back some of the professional firms' charges in the Nortel proceeding, citing errors or inadequate disclosure.

And the U.S. has initiated an overhaul of the rules governing law firms' disclosure of fees and expenses in major Chapter 11 bankruptcy cases, although the changes do not apply to Nortel because the company filed for protection in the U.S. before the rules came into effect last November.

In Canada, "judges have questioned the size of legal bills but have not done anything to control these costs," said McAvoy.

Law firms and other professionals say they charge fair market rates for the highly specialized skills needed to value and disburse assets from Nortel's far-flung empire, and have provided disclosure of fees and other charges throughout the process.

The expensive legal work has also produced benefits such as a \$75-million settlement with British and European creditors of \$1.77 billion in claims against Nortel assets.

And law firms say they have taken steps to limit costs.

Torys LLP, for example, special Canadian counsel to debtors, said work has been performed by those most familiar with the matter and by the "lowest-hourly-rate professional (who is) appropriate."

The international firm, with offices in Toronto, added that it has co-ordinated with U.S. counsel Cleary Gottlieb and others in the case to minimize duplication.

In its requests to the courts for compensation, Torys said it has “endeavoured to represent the debtors in the most expeditious and economical manner possible.”

Torys’ 14th quarterly fee application, filed this month, requested \$2,298,647 (U.S.) in fees, including nearly \$1 million for April.

Lawyers also point out that this is not a typical bankruptcy.

Nortel’s global footprint created a particularly complex corporate web that included operating divisions employing tens of thousands of people in the U.S., Europe, the Middle East and Africa, and at its head office in Canada.

Besides professional fees, the estate’s value has declined because of pretrial settlements with creditors in Europe and the U.S. It has also been depleted by salaries and retention bonuses paid to fewer than 30 employees who have stayed on at Nortel to help manage the company’s marathon bankruptcy process.

In its heyday in the late 1990s, the digital networking equipment maker had more than 95,000 employees, a market value of \$250 billion and a reputation as a leading research hub controlling patents on some of today’s most widely used wireless technologies.

But the company amassed debt with an acquisition spree to build up its optical gear sales, and the dot-com implosion of 2001 dried up demand for its products.

After a damaging accounting scandal, Nortel filed for protection on Jan. 14, 2009, leaving myriad creditor groups with aggregate claims on the estate totalling more than \$36 billion.

Nortel auctioned off most of its assets in 2011 to help build an escrow fund to pay a portion of what it owed to bondholders, trade suppliers, governments and banks that supplied loans, and former workers, with employees well back in the queue as unsecured debtors.

U.S. bondholders are seeking the lion’s share of the assets to cover their investment in Nortel during the late 1990s. The former Canadian employees and other creditors to the Nortel Canada estate, meanwhile, are seeking \$2.51 billion (Canadian). McAvoy said he doesn’t expect to receive more than 10 cents on the dollar.

Most of the cash generated by auction came from 6,000 patents covering wireless and Internet technologies ranging from mobile standards to search and social networking.

The patents fetched \$4.5 billion (U.S.) after several rounds of bidding — well above what was expected.

Final written submissions by debtors and other parties are expected in the fall, so a ruling may not be handed down until next year.

In the U.S., steps have been taken to rein in the Nortel fees, such as the imposition of a 10-cents-a-page cap on photocopying expenses from outside firms, said a spokeswoman for the U.S. Trustee Program, which monitors bankruptcy.

She also said the trustee has reviewed bills and occasionally negotiated a “voluntary reduction,” such as the paring of \$12,069 in fees and \$448 in expenses on an \$866,563 monthly bill in 2013 from unsecured creditors’ co-counsel Akin Gump.

A preliminary report from a fee examiner appointed to the Nortel case in the U.S. detailed 37 time entries in which, it said, the task and time description did not match hours charged by the business law firm, whose largest office is in Washington, D.C. Akin Gump did not respond to a request for comment

The examiner, accounting firm Master, Sidlow & Associates, also “recomputed” an invoice from lead U.S. debtors’ counsel Cleary Gottlieb to reduce a \$23-million bill for three months ending on Jan. 31 by \$3,182.

More than 150 legal professionals at Cleary Gottlieb logged 40,475 hours of billable work at rates as high as \$1,165 per hour over the period.

Spokespersons for the firm and the examiner did not respond to a request for comment, but in court filings, New York-based Cleary Gottlieb cited “inadvertent errors” in the bill.

Trustee Program spokeswoman Jane Limprecht said that the new U.S. rules, announced amid mushrooming costs and allegations that firms take advantage of insolvency cases, call on U.S. attorneys to submit budgets estimating the cost of the work they intend to perform.

The eye-popping professional services tab in the Nortel bankruptcy includes scores of huge invoices from blue-chip business law firms, but it also comes down to nickels and dimes.

Billable hours for lead counsel including Goodmans LLP, Koskie Minsky LLP and Gowling Lafleur Henderson LLP in Canada are key contributors to the tab, but the Nortel case file also shows charges of as little as eight cents by U.S. firms for mundane expenses such as failed audio conference connections.

Goodmans and Gowling did not respond to a request for comment.

Firms have invoiced for a few minutes to review emails, and court records reveal arguably steep rates for junior practitioners used in the U.S., such as \$405 for a one-year associate compared to a more typical fee of under \$200.

With more than 100 participants in the complex legal battle, even monthly copying and delivery expenses have reached the stratosphere:

- In one three-month invoice, Cleary Gottlieb billed the estate more than \$73,000 in duplicating charges as part of an \$18.4-million bill for fees and expenses through April 30.
- In 2012, Lisa Schweitzer, a high profile cross-border bankruptcy partner at the New York firm, billed Nortel \$2,600 for a two-and-a-half-hour meeting to discuss employee issues.
- In some instances, law firms have asked the U.S. court to approve \$100,000 or more to cover costs for preparing monthly billings.

Professional fees are paid out in interim amounts as the process unfolds. As of March, professional fees charged to Nortel and approved by the courts amounted to \$374 million in Canada, \$492 million in the United States and \$319 million in Europe, the Middle East and Africa, according to independent financial analyst Diane Urquhart, who is assisting retirees and ex-staff pro bono.

Urquhart said the retirees' last hope is that Judge Kevin Gross in the U.S. or Ontario Superior Court Justice Frank Newbould in Toronto will order a clawback of the fees during the evidentiary portion of the Nortel bankruptcy trial, which is expected to wrap up by the end of this month.

She said there is precedent for a cap or across-the-board reduction, which could be ordered by the courts without any finding or implication of wrongdoing.