

Speech at CAW & NRPC Pension and Severance Rally at Queen's Park

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The old saying that everyone compromises in bankruptcy, just isn't true anymore. Hedged junk bond owners and private equity plunderers are profiting from the demise of companies. Insolvency lawyers and accountants are happy to attend the Irish wake for the deceased company. These wakes go on and on, with the taxi meter running.

It seems that its only Canadian pensioners, long term disabled and severed employees, who lose in bankruptcies. The United States and the United Kingdom provide well over \$50,000 per annum of public pension and disability insurance to its citizens. To add insult to injury, the U.S. and U.K. governments are asking Nortel Canadian pensioners, disabled and severed employees to compensate them for the pension guarantees they gave their citizens.

Alex MacFarlane of Fraser Milner Casgrain, is the Canadian lawyer for the Official Committee of U.S. Unsecured Creditors. He represents the U.S. Pension Benefit Guarantee Corporation in this role. At the Appeal Court of Ontario on October 1st, Mr. MacFarlane argued that Canada has no money and all payments, including Canadian statutory severance, need to be stayed. He emphasized it's

important to leave the money in the various jurisdictions where it's currently sitting – there should be no transfer payments between jurisdictions.

A country and western singer knows what it means to be broke: your wife's gone, your dog's dead and the bank has taken your truck back. Nortel's not broke. It has US\$2.6B cash in the bank now and the 5 business sales will raise its cash balance to US\$6B . By mid January 2010, Canada's cash cupboard will be empty. The U.S. and U.K. estates have hoarded all the cash in their own countries. The Canada estate's R & D and head office costs are being financing by borrowings from the foreign divisions. The U.S. and U.K. governments and the powerful U.S. junk bond holders are fighting vigorously to limit the amount of Nortel business sale proceeds that Canadian pensioners, disabled and severed employees will get. If children treated their elderly parents this way, it's called elder abuse. Yet no Canadian government is at the negotiating table to push back on the powerful creditors at international subsidiaries, that Nortel spawned over its 115 year history as a successful Canadian company.

The volleyball game between Canadian and Ontario governments on the Nortel bankruptcy file is going to reduce employee benefits for all Canadians. Continuing inaction is a policy to reduce the standard of living for all Canadian workers and retirees. Continuing inaction is a clear signal that fixed income speculators and private equity investors have more influence on Canadian governments than Canadian pensioners, disabled and severed employees.

Premier Dalton McGuinty announced in April 2009 that the Ontario Pension Benefit Guaranty Fund is broke and Ontario will not cover pension liabilities should another major company fail. The Ontario government has a moral obligation to pay for the deficit on the first \$1000 per month of pension income for the companies that paid premiums to the Ontario Pension Benefit Guaranty Fund. It should loan the Pension Benefit Guaranty Fund the money and raise premiums from the participating companies to repay the loan.

Federal Industry Minister Tony Clement is disingenuous when he tells the Federal Parliament that pension benefits are the responsibility of the Provincial Government where the pension fund is registered. The Federal Government says it will protect the Federally registered pension plans. But it is the Federal bankruptcy laws that oust Provincial pension benefit and severance laws. It is the Federal BIA that needs fixing to ensure companies cannot choose to avoid paying their employment obligations under Provincial law.

Fortunately Canada is a democracy. Our votes decide our governments' policies. I personally believe that your presence at Queen's Park today is a turning point. Our grass roots campaign will ultimately prevail over the backroom lobbying going on to stop the BIA amendment for preferred status to employment related claims.

There are 5.5 million members of defined benefit pension plans in Canada. The Office of the Superintendent of Financial Institutions estimates 83 per cent of

federally-registered defined benefit pension plans were under-funded in December 2008; up from 71 per cent just six months before. Provincially-registered pension plans are similarly underfunded.

1.0 million Canadians are members of self-insured long term disability plans. All working Canadians want severance protection.

Add Cassels Brock to the list of Bay Street law firms lobbying against the BIA Amendment for preferred status of employment related claims. The firm recently spoke out about the new super-priority provision for \$3000 of unpaid wages and severance that was given Royal Assent on September 18th. It says the new amendment "will have serious and unknown consequences to our credit markets at a time of particular distress by reducing credit availability."

Where was this law firm when its investment banking clients packaged US subprime and high risk credit default swaps into \$32 billion of toxic Non Bank Asset Backed Commercial Paper sold to Canadians. ABCP has caused \$22 billion of damages to Canadians. Bay Street lawyers missed the ABCP debt problem, but they're ever vigilant about the serious debt market consequences from paying a working person less than one month of severance pay!

I have looked everywhere for research on the subject of how preferred status in bankruptcy affects the cost of debt. I asked numerous Canadian and U.S. fixed

income portfolio managers and company CFO's if they had ever seen such research and they could not refer me to any. I finally found a March 2002 study from the Government of Canada Parliamentary Research Branch and it has the following to say:

"Granting a super priority to unpaid wages and other employee entitlements would affect the priority position of secured creditors and likely increase the cost and/or reduce the availability of credit. Indeed, past attempts to introduce a super priority were strongly opposed by credit grantors and businesses alike for these very reasons and, as was recently suggested, there would appear to be no evidence that this opposition has weakened."

Well well. The Federal bureaucrats are persuaded by the strong opposition of the credit grantors and businesses. Yet, the government's report contains no evidence to support that preferred status will materially raise the cost of debt.

I decided to do my own analysis on the cost of debt based on my in-depth knowledge of how bonds are valued and using Moody's statistics on the frequency of corporate bankruptcies and cash settlement ratios. I have determined that the impact of the BIA amendment on the overall cost of debt capital is a minimal 0.05% per annum for investment grade bonds. The cost for junk bonds is a bit higher at 0.25% per annum . The cost increase is much lower if I were to take into account recoveries from bond insurance.

So let's say a company has \$100 million of junk bonds, an extra 0.25% annual interest costs is \$200,000 per year after tax. The reason the impact of the preferred status on the cost of debt is so low is because there's only a small percentage of large companies that go bankrupt.

The BIA amendment cannot be harming Canada's international competitiveness. It's Canada that has the unfair cost advantage of not needing to protect its retirees . U.S. and U.K. companies are forced to pay premiums for the U.S. and U.K. public pension and disability insurance plans.

For companies that do file for bankruptcy, employment claims getting preferred status would leave little left for the junk bond holders. However the damage can be mitigated by keeping pension plans fully funded with a cushion for economic downturns. A large percentage of junk bond owners own credit default swaps, where the counterparties reimburse the credit default loss. Other distressed debt buyers like, Matlin Patterson, are working from very deep pockets. They buy the junk bonds at cents on the dollar. They make up for their lemons with occasional big payoffs. For every ten distressed investments his firm makes, one to three of them will be the big money makers for the fund.

Chrysler secured creditors were forced by US governments to take pain for the benefit of workers harmed by this economic crisis. Most of the bond owners were willing to accept their loss. The U.S. Supreme Court refused to hear the case

of the small minority of secured bond holders who wished to contest the illegality of Chrysler giving restructuring plan value to the Chrysler employees.

On May 1, 1998, John Roth, former CEO of Nortel, wrote a letter to his employees saying: " Nortel provides a solid safety net aimed at protecting you and your family in the event of illness, injury, disability or death." John Roth knew his future was taken care - he took home \$159 million from 1999 to 2001.

The greed of one man would have paid for close to all of the income needed by Nortel's disabled employees now. Jackie Bodie has Parkinson's . Her CPP disability income at \$13,300 per year won't cover both a roof over her head and food on the table – guess she'll have to pick one. Had Jackie known that Nortel's plan was self-insured, she would have bought personal LTD insurance – now, it's too late. Only Alberta and B.C. require that companies disclose their LTD plan is self-insured and not fully funded.

Josee Marin is a single mother with a son. She has scleroderma - a serious skin disease, Crohn's disease and asthma. She finally got a loan to purchase a house. She moved into the house the day that Nortel declared CCAA protection. Now she loses this security for herself and son. Self-insured LTD plans have been a known problem since 1985, when Massey Ferguson declared bankruptcy and left its disabled employees destitute. Our country presents itself to the world

as socially responsible and a defender of human rights. Yet we do not protect the pensions of our seniors and provide basic security for the disabled.

The Nortel case is a precedent for a line up of Canadian companies who choose to sell their businesses under bankruptcy protection, trigger credit default swap cash settlements and walk away from their obligation to pay employee benefits.

Lyndon Barnes of Osler Hoskin Harcourt gave an emotional presentation on behalf of the Nortel Directors at the October 1st severance appeal. Nortel paying statutory severance effectively gives employees “super priority”. This, he argued, could only be done by Parliament and not by judicial decisions.

We are asking Parliamentarians not to use the excuse that the matter is before the court. Both the Federal and Ontario governments need to step to the plate to fix the glaring holes in Canada's safety net for pensioners, disabled and severed employees. Surely, our governments are not willing to protect the interests of junk bond speculators and unregulated credit default swap players over the well-being of Canadians!