Urquhart

Subject: FW: Coffee at Timothies Tomorrow @ 10:30 A.M.

From: Kosarenko, Roman [mailto:Roman.Kosarenko@bmo.com]
Sent: September-21-10 2:09 PM
To: 'Urquhart'
Subject: RE: Coffee at Timothies Tomorrow @ 10:30 A.M.

Diane,

I am not a specialist in taxation, so I can't respond to your questions. Whatever I know about relative allocation of funds in the financial statements is heresay. I only dealt with contributions at the aggregate, trust level. Current tax rules may not eb relevant as the bulk of the assets in the HWT was contributed in early 1980s. I think at the time, CRA allowed deductions for full amount of contributions, but the rules since changed around 1985 and there was no more tax advantage to operating a HWT, other than the partial offset of the LTD expense with investment income.

I also know that Nortel had a policy of keeping the LTD section of the HWT funded at 40%, while the PIF was funded much better (be design). Given that the DB plan was closed to new members since 1999 or 2000, I don't recall any new contributions to the PIF during my time at Nortel Treasury. I think the PIF was viewed as a self-sustained run-off vehicle.

Again, for allocation of funds, the best source of information is Fabrice Jestin or Tony Gosio.

Regards,

Roman Kosarenko, CFA
Senior Manager, Pension Investments
BMO Pension Fund Society
Tel (416) 643-1726

From: Urquhart [mailto:urquhart@rogers.com]
Sent: September 21, 2010 01:48
To: Kosarenko, Roman
Subject: RE: Coffee at Timothies Tomorrow @ 10:30 A.M.

Roman

Thank you for meeting me this morning and making this follow-up note.

Carol is looking for your USB stick, but is not optimistic about finding it. Probably left it in her old desk.

You are right that the Nortel HWT trustee agreement specified a list of benefit plans as noted in the excerpt from it below.

It seems to me that the active employees medical and dental benefits would be covered in "A Health Care Plan" and the definition of "employees" covers actives.

I agree with you and see that Nortel treated four plans as funded: retiree life insurance, member-paid optional life insurance, LTD and SIB/STB, as you say. We will be arguing that what Nortel management did in book-keeping does not formulate a legal obligation to do so. It may have been doing voluntary partial pre-funding.

I also agree that what Nortel told its employees about life insurance coverage in their brochures and communications is relevant to legal obligations too. We are studying the Nortel retiree brochures and communications again looking for statements about there being a Pensioners Life Insurance Fund, a Health and Welfare Trust containing assets to fund the Pensioners Life Insurance, or any other wording that suggests a Nortel commitment to fund its promise to provide post retirement insurance coverage.

Joann Williams, an actuary from Welton Parent Inc. , Ottawa is using the legal argument that the Nortel Pensioners Life Insurance Plan must be considered to be a Group Life Insurance Plan, since this is what is covered in the Nortel HWT trustee agreement. As noted in her email to me below, she further argues that the Nortel Pensioners Life Insurance Plan must be within the terminology of "group term life insurance policies" as this is the only type of life insurance permitted in HWTs according to the CRA Rules for the types of benefit plans that can be within HWTs.

I HAVE SOME QUESTIONS ABOUT THE TAX REASONS.

It would be helpful to me (an advocate for the Nortel disabled who are all very sick) to know more about what you are saying in this phrase:
"For tax reasons, the portion of the HWT assets designated for life insurance could only be used for life insurance. "

Joann Williams has this to say in her email below on tax point:

"If the employer took tax deductions for those contributions when they were made and no taxable benefit was received by the retirees at the time the contributions were made, then they could not have been made in respect of retirees.

Ideally we would like to show that Nortel calculated its total bona fide HWT contributions correctly (as shown on its tax returns) but then made notional allocations that did not reflect the various components of the calculation."

Are you saying by your point that Nortel put employer contributions into the HWT to pre-fund future life insurance premiums for its Pensioners Life Insurance Plan, beyond the amount of life insurance premiums paid in the current year and that the pre-funded portion of these life insurance premiums for future life insurance premiums was a taxable expense for Nortel each year? Is this why Nortel designated HWT assets for life insurance in its book-keeping for the Pensioners Insurance Fund and specified a separate reserve asset accounts for Pensioners Life Insurance in the HWT Financial Statements?

Or do you think that Nortel was allowed by CRA to pre-fund future life insurance premiums for its Pensioners Life Insurance Plan in the HWT, but in doing so it created a pre-paid expense, and was not allowed to make a tax deduction for the pre-paid amounts in the current year, only allowed to make the tax deductions in the future years when the life insurance premiums were actually paid to the insurance company?

If it was the first scenario of Nortel making tax deductions annually for both the current year pensioners life insurance premiums and the pre-funding of future life insurance premiums, do you think that the CRA cares if the Nortel HWT distribution takes these accumulated employer contributions within the HWT and used them to make an HWT settlement for the LTD Income beneficiaries, for which Nortel made did not make employer contributions in the past to fund the LTD income benefits?

If the pensioners did not expect that their pensioners life insurance to be pre-funded (we are checking the retirees brochures again here), while the LTD income beneficiaries were told in the actives brochures that their income benefit was self-insured and that Nortel played the role of an insurance company, what' s wrong with the HWT assets going to the LTD income beneficiaries and not to the pensioners who were promised a vested benefit but not promised a pre-funded one through the HWT?

Nortel - Montreal Trust H & WT Trustee Agreement Jan. 1, 1980.pdf

WHEREAS:

1. The Corporation has established for the benefit of certain of its employees and the employees of such affiliated or subsidiary Corporations as the Corporation may designate, certain Health and Welfare plans, and such other similar plan or plans as the Corporation may from time to time place in effect, as follows:

a) a Health Care Plan;

b) a Management Long Term Disability Plan;

c) a Union Long Term Disability Plan;

d) a Management Survivor Income Benefit Plan;

e) a Management Short Term Disability Plan;

f) a Group Life Insurance Plan;

all of which are hereinafter collectively referred to as the "Health and Welfare Plan".

4. The term "Employees" shall mean those active and retired employees of the Corporation and

3

designated affiliated or subsidiary corporations which have adopted the Health and Welfare Plan, including dependents as defined in Schedule A, on whose behalf contributions are or have been made to the Trust Fund and who are eligible for benefits under the Health and Welfare Plan.

6. The term "Trust Fund" as used herein shall mean all of the assets of the "Health and Welfare Trust" including all funds received by way of contributions from the Corporation and those of its designated affiliated or subsidiary corporations in accordance with the provisions of the Health and Welfare Plan and of this Trust Agreement, and all employees' contributions together with all profits, increments, and earnings thereon.

From: Joann [mailto:joannwilliams119@hotmail.com]
Sent: September-13-10 11:37 AM
To: 'Urquhart'; 'Joel Rochon'; 'Sakie Tambakos'; 'John Archibald'
Cc: 'Jeremy Bell'
Subject: RE: Nortel: Update and Nortel HWT Charts - Draft # 3

Hi all,
I don't think this matter turns on actuarial standards in isolation; they are useful only to the extent that they illuminate other factors of a legal nature.

The main point about HWTs is that they may only consist of:

a) group sickness or accident insurance plans

b) private health services plans

c) group term life insurance policies, or

d) any combination of a) to c).

We need to emphasize that the retiree life reserve does not fit into this structure. A bona fide HWT, as defined by CRA, may purchase term life insurance for the retirees, but not hold assets in respect of future life insurance. Such funds should have been given to an insurance company to extend the term of the life insurance for the retirees under a bona fide HWT.

If the employer took tax deductions for those contributions when they were made and no taxable benefit was received by the retirees at the time the contributions were made, then they could not have been made in respect of retirees.

Ideally we would like to show that Nortel calculated its total bona fide HWT contributions correctly (as shown on its tax returns) but then made notional allocations that did not reflect the various components of the calculation.

In summary, I think our strongest argument would be (something like) the liability of the HWT on wind up, or any other time, in respect of retiree life insurance does not exceed the outstanding group term life insurance premiums. This is because of tax considerations that apply regardless of any ambiguous wording of the trust document.

Joann

Sincerely

Diane A. Urquhart
Independent Financial Analyst
Mississauga, Ontario

Tel: (905) 822-7618
Cell: (416) 505-4832
E-mail: urquhart@rogers.com

From: Kosarenko, Roman [mailto:Roman.Kosarenko@bmo.com]
Sent: September-21-10 12:01 PM
To: 'Urquhart'
Subject: RE: Coffee at Timothies Tomorrow @ 10:30 A.M.

Diane,

Based on our conversation, I may be able to help you ascertain the nature of the additional deficit created by the HWT funding moratorium (at the trust level).

The review of the HWT was initiated in spring of 2005, with the goal of winding down the trust if possible (with Nortel assuming both assets and liabilities of the trust). The formal head of the review team was Mike McCorkle. For the duration of the review, contributions were suspended. Over the course of the review, it was determined that Nortel would have to top-up any deficit in the HWT for a proper termination of the trust. The other obstacle was the necessity to update the trust agreement and a wait-out period of about 5 years to ensure that the changes are not seen as tailor-made for termination of the trust.

After the review, Nortel resumed contribution with a 12-month lag, versus the normal 2 month lag. Monthly contributions were about $3.2-3.5 million. I made sure that the exact amounts were contributed (e.g. the amount contributed in April of one year was exactly equal to the amount calculated for April of the year before), so that there is no uncertainty about the existence and the nature of the lag.

In the next 2 years, life insurance surpluses were retained in the HWT (although they could have been sent to Nortel). Under a self-insurance scheme with Sun Life, Nortel/HWT would remit to Sun Life any excess of claims over premiums every year (for the past year) and receive any surpluses from Sun Life. These surpluses were significant, so the contribution lag shortened to 11 and then 10 months worth of contributions.

Current amount of required contributions were calculated in a usual manner (without a delay). The amount “Due from sponsor” in the financial statements of the HWT, I believe, includes only a portion of the contributions that relates to funded plans.

With regard to arguing the claim of LTD recipients versus that of the pensioners, I don't think I can help. Your best source in terms of actual practice is Fabrice Jestin (not Justin), who now lives in Ottawa, or his predecessor Anthony Gosio, who retired from Nortel 4-5 years ago, and should live in the GTA area. They were compiling monthly reports on contributions to the HWT, with break-down plan by plan. Which of the plans are funded and which are not is open to legal interpretation, but the actual practice can point to what Nortel considered funded versus unfunded. Also, Carol Tkaczyk may still be in possession of the USB key with my files, including some of those reports, or she may know who has it.

I don't have HWT trust documents to refresh the memory, but I believe that of the 9 or so benefit plans, Nortel treated four plans as funded: retiree life insurance, member-paid optional life insurance, LTD and SIB/STB. For tax reasons, the portion of the HWT assets designated for life insurance could only be used for life insurance. The SIB/STB component was relatively small. So, the main "donor" of the loan to Nortel, from the accounting & tax point of view, was the LTD section of the HWT. The largest unfunded plan was dental & medical for active employees - I don't believe it was the part of the original trust agreement, please check your documents to confirm.

Regards,

Roman Kosarenko, CFA
Senior Manager, Pension Investments
BMO Pension Fund Society
Tel (416) 643-1726

From: Urquhart [mailto:urquhart@rogers.com]
Sent: September 20, 2010 02:18
To: Kosarenko, Roman
Subject: Coffee at Timothies Tomorrow @ 10:30 A.M.

Hi Roman

Thank you for agreeing to talk with me over coffee tomorrow. I will be speaking to Mike McCorkle about our conversation tomorrow night. As you know Mike has gone on to become the Treasurer of The Bay. He is willing to prepare a sworn affidavit about what was happening at the Nortel HWT from his perspective as an Assistant Treasurer and later Acting Treasurer and as one of the executives on the Nortel Pension Investment Committee between 2005 and 2008.

He wanted me to speak to you first on what you remember to be the conceptual approach the HWT took in terms of a number of issues I discussed with him this weekend.

The Nortel long term disabled employees, who I am working with, are full of fear and stress about their futures. If you can help me in any way, it would be a significant goodwill contribution by yourself to help these very sick and injured people. I can think of no negative consequences for you personally as this is simply a technical legal process to get about $ 36 M more out of the HWT and another $50 M out of the Nortel estate, which by the way is expected to have $6 B for disbursement to the creditors.

Here are the questions I have of you and I certainly would not expect you to remember specific dollar amounts. I, and now Mike, want to understand why the HWT financial statements and actuarial reports look the way they do in context to what the management decision-making was at the time. I have put some summary slides together about the Nortel HWT from information that is now public from court documents.

- How in general terms were the employer contributions calculated for the Pay as You Go Pensioners, LTD and Active Medical Claims and the LTD and Actives Life Insurance Premiums?

- How in general terms were employer contributions calculated for the Funded LTD Income and the Survivor Income and Transitional Benefits ?
  (There was a change in HWT Financial Statements methodology in 2007 to remove the employer contributions and claims paid for the Pay As You Go Medical and Life Insurance Benefits, except for the Pensioners Life Insurance Premiums that continued to be paid out for the HWT assets. These PAYGO benefits became payable directly by Nortel and not through the HWT.)

- How did Nortel perceive its obligation to pre-fund the Pensioners' Future Life Insurance Premiums? The earlier sense of obligation to pre-fund Pensioners' Future Life Insurance Premiums seemed to be dropped in 2003? Were you there then?

- How were the employer contributions recorded in the HWT financial statements for the 2005-2006 moratorium period when Nortel stopped making employer contributions for the Pay as You Go Pensioners, LTD and Active Medical Claims and the LTD and Actives Life Insurance Premiums

- Do you think the "Due from Sponsor Company" includes an IOU for the employer contributions not paid during 2005-2006 moratorium for the Pay as You Go Pensioners, LTD and Active Medical Claims and the LTD and Actives Life Insurance Premiums? In other words, would I be double-counting if I expected the creditors of Nortel to fully repay the "Due from Sponsor Company" Note and the withdrawn employer contributions during the 2005-2006 moratorium?

- Or is this "Due from Sponsoring Company" a distinct matter in the form of an IOU for the employer contributions that Human Resources calculated for the funding of the LTD Income and the Survivor Income and Transitional Benefits? This "Due from Sponsor Company" accounts receivable has been going on since 1980 and therefore is not a new accounting entry to cover the need to repay the 2005-2006 moratorium of employer contributions for the Pay As You Go Benefits.

- How did Human Resources determine the mix between the employer contributions paid in cash versus those that were "Due from the Sponsor Company"?

I look forward to meeting you tomorrow.

Sincerely

Diane A. Urquhart
Independent Financial Analyst
Mississauga, Ontario
Tel: (905) 822-7618
Cell: (416) 505-4832
E-mail: urquhart@rogers.com