



May 31, 2006



LETTER OF COMMENT NO. 86

Suzanne Bielstein
Director of Major Projects and Technical Activities
Financial Accounting Standards Board
401 Merritt 7
PO Box 5116
Norwalk, Connecticut 06856-5116

File Reference No. 1025-300

RE: Exposure Draft "Proposed Statement of Financial Accounting Standards Employer's Accounting for Defined Benefit Pension and Other Post-Retirement Plans an amendment of FASB Statements No. 87, 88, 106, and 132(R)"

Dear Ms. Bielstein.

Nortel Networks, Inc. (Nortel) is a publicly traded corporation and a global supplier of communications equipment, software and services, serving both telephone service provider and business enterprise customers. While we are headquartered in the Greater Toronto Area, our securities are traded on the New York Stock Exchange (in addition to the Toronto Stock Exchange), we follow accounting principles generally accepted in the United States of America, and we file Annual and Quarterly Reports on Forms 10-K and 10-Q with the Securities and Exchange Commission. We have company-sponsored defined benefit pension plans and other post-retirement plans in numerous countries. Nortel supports the Board's attempt to improve the transparency and understandability of the costs and obligations of providing post-retirement benefits and appreciates the opportunity to comment on the proposed Statement. Our principal comments regarding the recognition of the projected benefit obligation and compression of the measurement date are summarized in the body of this letter and we have attached an Appendix containing responses to the specific issues raised in the Notice for Recipients.



Projected Benefit Obligation

The recognition of unrecognized actuarial gains and losses and unrecognized prior service cost as a component of other comprehensive income is a significant step in bringing transparency to the financial statements; however, the recognition in the financial statements of a projection, that is, a projected benefit obligation that includes future increases in compensation as a component of its measurement, does not result in an accurate picture of the true liability as of the balance sheet date. Future salary increases do not represent promises made to employees and are not "present obligations" of the employer, as required under the definition of liabilities in Statement of Financial Accounting Concepts No. 3, paragraph 35.

We note this measurement issue has been excluded from the scope of the proposed Statement and will be included in the second phase of this project. We urge the Board to reconsider this decision, out of respect for users of financial statements as well as its own due process. It would create significant confusion for users to see obligations based on one measurement today and potentially another measurement several years from now. Further, the discussion of this scope decision in the Basis for Conclusions is troubling in several respects. First, the assertion is made in paragraph B16 that the proposed Statement does not change the basic approach to measuring benefit obligations, when this aspect of the "basic approach" is used only for disclosure. Second, the discussion in paragraph B17 seems, by quoting paragraph 139 of Statement 87, to stigmatize those with concern about the validity of this measurement by linking them to those who argued against accrual accounting for pensions over twenty years ago.

To illustrate our perspective on the measurement issue, a North American company could assume salary increases in future service years to estimate the projected benefit obligation as of a balance sheet date of December 31' 2006. For 2007, the company may decide to freeze the plan at current salary levels, which would reduce the projected benefit obligation. Such a unilateral decision, which is becoming increasingly common in North America, would not change the present obligation of the employer because the employer has no obligation to provide the underlying future salary increases.



Like the projected benefit obligation for pensions, the accumulated post-retirement benefit obligation (APBO) for non-pension post-retirement benefits includes a portion that does not meet the definition of a liability. The APBO includes non-vested liabilities that can be taken away by an employer and therefore do not represent present obligations. For example, an employer can unilaterally decide to terminate a post-retirement medical plan, which action is also becoming increasingly common in North America. Employees are not vested in those benefits and this would result in an immediate reduction in the APBO for a unilateral action that is not a change in a present obligation.

Measurement Date

As stated earlier, Nortel has numerous individual defined benefit plans and other post-retirement plans globally that are consolidated for reporting purposes. These plans have measurement dates that differ from the date of our financial statements as allowed under Statement 87. We have polled our service providers, including asset trustees and actuaries, to determine the amount of time required to prepare the year end accounting information, and have determined that it will be extremely difficult to use a measurement date that coincides with our financial reporting date of December 31st and still meet the accelerated 60-day filing deadline for our 2007 Annual Report on Form 10-K to the SEC, as discussed in more detail below.

While some work can be performed prior to the measurement date, the discount rate, asset values, and cash flows cannot be obtained until the measurement date. It has historically taken between 15 and 20 days after the measurement date to receive the fair values of plan assets from the trustees. It takes an average of 7 days after the measurement date to calculate and analyze the discount rate using cash flow matching techniques suggested by the SEC and an additional 5 - 10 days for the actuary to calculate the obligation using the approved discount rate. At the earliest, Nortel would have the information to record the year end assets and obligations 20 days after the measurement date. All analysis of the information, recording of the entries, and external audit of the calculation would take place late in the year-end reporting cycle leaving very little time for a complete and thorough analysis of the data. This challenge is compounded by having multiple defined benefit plans in multiple countries.



After the obligation and assets are properly recorded, the disclosure would need to be prepared. Our actuaries have informed us that would take another 10 - 15 days to provide the remaining disclosure information. Nortel would then have to consolidate the global information and prepare the disclosure, which would be ready approximately 40 days after year end using the actuaries' timelines. The external audit and SOX certification of that disclosure would then need to be completed. As a comparison, this information is currently available 20 days after year end for external audit and external reporting purposes.

The above timelines assume the actuarial community has adequate resources to prepare the information for all their clients with a December 31st year end, which we seriously doubt, but about which we urge the Board to Inquire. Our experience has been that any change to the normal annual calculations especially related to Statement 88 accounting for curtailments, settlements, and/or contractual or special termination benefits requires a reprioritization and reallocation of resources by the actuaries, further challenging the timeliness of SEC filings. Further, the cost implications of the industry-wide adjustment the Board would have the actuarial community undertake are chilling.

The obligation calculation is a highly complex calculation that currently requires much preparation and analysis to ensure accuracy and timely reporting. Obviously, the timelines laid out above are not acceptable for the collection, processing, and validation of data. In order to achieve the multiple objectives of shortening the timelines, ensuring accuracy of the calculation and enabling timely filing with the SEC, new approaches would need to be adopted. One approach could be adopting a two-stage process, in which detailed calculations are undertaken prior to year-end followed by a more approximate roll-forward and adjustment at the actual year end. This two-stage process would require more time and cost than a single calculation, but allow any issues to be flushed out at an early stage. In some instances the asset fair value data may need to be extrapolated from part-year figures and benefit payments may need to be estimated, which compromises the accuracy of the data and contradicts the main goal of using a year-end measurement date. If this provision of the proposed Statement is adopted, it should be explicitly noted in the Statement that estimates and extrapolations are part of the process, so there is no question as to the trade-off required in using a measurement date that coincides with the financial



reporting date. As a separate point, we do not believe this trade-off a wise one and are particularly concerned about attempting it in a Sarbanes-Oxley world where the need for a non-trivial audit adjustment can be an internal control issue, thus opening the door to further internal control and other financial reporting problems.

We appreciate the opportunity to comment on the proposed Statement. If you would like to further discuss any of our comments, please do not hesitate to contact me at (905) 863-3653 or pkarr@nortel.com.

Sincerely,

Paul W. Karr

Controller

Nortel Networks, Inc.

C: Michael S, Zaffrofsky, President and Chief Executive Officer
Peter W. Currie, Executive Vice President and Chief Financial Officer



Appendix

The following addresses the specific issues raised in the Notive for Recipients.

Costs of Implementing the Proposed Statement's Requirement to Recognize a Plan's Overfunded or Underfunded Status in the Employer's Statement of Financial Position

Issue 1: The Board concluded that the costs of implementing the proposed requirement to recognize the overfunded or underfunded status of a defined benefit postretirement plan in the employer's statement of financial position would not be significant. That is because the amounts that would be recognized are presently required to be disclosed in notes to financial statements, and, therefore, new information or new computations, other than those related to income tax effects, would not be required. Do you agree that implementation of this proposed Statement would not require information (other than that related to income tax effects) that is not already available, and, therefore, the costs of implementation would not be significant? Why or why not? (See paragraphs B20-B34 for the basis for the Board's conclusions.)

Response 1: We agree that the information needed to record the amounts that would be required under the Proposed Statement is available, so the narrow comment above on cost is correct. However, the discussion on Benefits and Costs in the Exposure Draft Summary, and in the Basis of Conclusions in the proposed Statement, understates the potentially substantial costs of compressing the measurement and financial statement dates, as discussed in connection with Issue 2 below. Further, the use of the adjective "certain" to describe the many companies that do not use the financial statement date as the measurement date betrays a lack of understanding of this widespread practice.

The Employer's Measurement Date

Issue 2: Unless a plan is sponsored by a subsidiary that is consolidated using a fiscal period that differs from the parent's, this proposed Statement would require that plan assets and benefit obligations be measured as of the date of the employer's statement of financial position. This proposed Statement would eliminate the provisions in Statements 87 and 106 that permit measurement as of a date that is not more than three months earlier



than the date of the employer's statement of financial position.

Are there any specific implementation issues associated with this requirement that differ significantly from the issues that apply to other assets and liabilities that are recognized as of the date of the statement of financial position? (See paragraphs B36-B40 for the basis for the Board's conclusions.)

Response 2: Substantial implementation issues, and attendant costs, would be created by compressing the measurement and financial statement dates. The details of these issues are included in the body of the letter above and summarized as follows:

- The measurement of these assets and liabilities contains a complexity that does not exist with other assets and liabilities.
- Discount rate, asset values, and cash flows cannot be obtained until the measurement date and it takes actuaries an estimated 20 days after the measurement date to finalize
- Disclosure data takes an additional 10 15 days for the actuaries to prepare
- Analysis, recording, consolidation, external audit, and SOX certification of the data recorded and disclosed must then take place
- Actuarial community must have adequate resources to handle volume at December 31st
- Reporting period would allow no room for complexity due to SFAS 88 accounting
- Timely SEC filings will be challenging
- Shortening of these timelines jeopardizes accuracy of calculation.

Effective Dates and Transition

Recognition of the Overfunded or Underfunded Status

Issue 3(a): The Board's goal is to issue a final Statement by September 2006. The proposed requirement to recognize the over- or underfunded statuses of defined benefit postretirement plans would be effective for fiscal years ending after December 15, 2006. Retrospective application would be required unless it is deemed impracticable for the reason discussed below.

An entity would be exempt from retrospective application only if the entity determines that it is impracticable to assess the realizability of deferred tax assets that would be recognized in prior periods as a result of applying the proposed Statement.



Should the Board provide an impracticability exemption related to the assessment of the realizability of deferred tax assets? Why or why not? Are there other reasons that retrospective application might be impracticable that the Board should be aware of? (See paragraphs B61–B64 for the basis for the Board's conclusions.)

Response 3(a): We do not have any objection to an impracticulity exemption related to the assessment of the realizability of a deferred tax asset. Retrospective application does require additional resources and we suggest limiting the retrospective period to 3 years allowing a company to provide more years of comparable data without having to restate all years in a five-year summary.

Issue 3(b): Some nonpublic entities (and possibly some public entities) may have contractual arrangements other than debt covenants that reference metrics based on financial statement amounts, such as book value, return-on-equity, and debt-to-equity. The calculations of those metrics are affected by most new accounting standards, including this proposed Statement.

The Board is interested in gathering information for use in determining the time required to implement this proposed Statement by entities that have such arrangements other than debt covenants. That information includes (a) the types of contractual arrangements that would be affected and what changes to those arrangements, if any, would need to be considered, (b) how the economic status of postretirement plans that is presently included in note disclosures is currently considered in those arrangements, and (c) how the effects of the current requirement in Statement 87 to recognize a minimum pension liability previously were addressed for those contractual arrangements. (See paragraph B65 for the basis for the Board's conclusions.)

Response 3(b): We do not have any contractual arrangements that include covenants that would be affected by this proposed Statement.

Measurement Date

Issue 4: This proposed Statement would require a public entity that currently measures plan assets and benefit obligations as of a date other than the date of its statement of financial position to implement the change in measurement date as of the



beginning of the fiscal year beginning after December 15, 2006. If that entity enters into a transaction that results in a settlement or experiences an event that causes a curtailment in the last quarter of the fiscal year ending after December 15, 2006, the gain or loss would be recognized in earnings in that quarter. Net periodic benefit cost in the year in which the measurement date is changed would be based on measurements as of the beginning of that year.

Are there any specific impediments to implementation that would make the proposed effective date impracticable for a public entity? How would a delay in implementation to fiscal years ending after December 15, 2007, alleviate those impediments? (See paragraphs B66–B69 for the basis for the Board's conclusions.)

Response 4: Specific and serious practical impediments are detailed in the body of this memo and summarized in response to Issue 2 above. Perhaps we misunderstand the question, but we do not understand shifting a requirement from years beginning after December 31, 2006 to those ending after December 31, 2007 to be a delay. In any event, a one-year delay in the effective dates will not solve the serious issues we have attempted to articulate herein.

Not-for-Profit Organizations and Other Entities That Do Not Report Other Comprehensive Income

Issue 5: This proposed Statement would apply to not-for-profit organizations and other entities that do not report other comprehensive income in accordance with the provisions of FASB Statement No. 130, Reporting Comprehensive Income, Paragraphs 7—13 of this proposed Statement provide guidance for reporting the actuarial gains and losses and the prior service costs and credits by those organizations and entities.

Do you agree that those standards provide appropriate guidance for such entities? If not, what additional guidance should be provided? (See paragraphs B53—B58 for the basis for the Board's conclusions.)

Response 5: As stated above, we do not support the guidance in the proposed Statement, but are not aware of any reason why the ultimate guidance should not be applied to such entities.